

Why the Rich Stay Rich. On dysfunctional institutions' "ability to persist" (no matter what)

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Abstract

This paper returns to the Ricardian tradition of understanding the distribution of income as the outcome of the political articulation of conflict between rentiers, capitalists, bureaucrats and labour - in which history, politics and institutions matter as much (if not more) than economic 'fundamentals'. Also, in this tradition economic underperformance arises mostly from the shift in distribution from operating profits to rents. The focus is on a key political economy question: why the rich stay rich, no matter what! This confirms the iron law of oligarchies: dysfunctional institutions tend to rebuild. In the case of Latin America, its élites' "ability to persist" relates to the fact that they have been able to enforce a "Southern-style" rule resembling a 'stationary process', whereby the unbalancing impact of shocks tends to have only limited life-spans -as oligarchies are able to landscape new scenarios to continue achieving their fairly immutable rent-seeking goals. They have used three main channels: forcing 'Buchanan'-style constitutional and legal straitjackets to restrict the scope of change; resourcefulness and collective action for reengineering their distributional strategies to suit the new scenarios, and cleverly absorbing elements of opposing ideologies (such as now accepting the need for 'social protection') to maintain theirs hegemonic. Their trump cards are ruthlessness in the first, and "jogo de cintura e jeitinho" (fancy footwork) in the other two. The analysis of these channels is the main subject of this paper.

Reference Details

CWPE 20124
Published 18 December 2020

Key Words income distribution, inequality, poverty, Palma ratio, "reverse catching-up", ideology, Gramsci, Foucault, neo-liberalism, 'new' left, institutional persistence, Latin America, Chile, emerging Asia, US, Western Europe

JEL Codes D31, E12, E22, E24, N16, N36, O50, P16

Website www.econ.cam.ac.uk/cwpe

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On dysfunctional institutions' "ability to persist" (no matter what)

José Gabriel Palma¹

[The national income]
is divided among three classes,
[rentiers, capitalists and labour] ...,
[in the form of] rents, profits, and wages.
To determine the laws
which regulate this distribution,
is the principal problem in Political Economy

David Ricardo

Inequality is a choice

Joseph Stiglitz

I am my choices

Jean-Paul Sartre

The comfort of the rich depends upon
an abundant supply of the poor

Voltaire

Cambridge Working Papers in Economics (CWPE) 20124

(Available at <http://www.econ.cam.ac.uk/research-files/repec/cam/pdf/cwpe20124.pdf>)

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A shortened version of this paper will be published (in Spanish and English) in *CEPAL Review*, 132, December

¹ Cambridge University and USACH (<http://www.econ.cam.ac.uk/people/emeritus/jgp5>). I am especially grateful to Alex Cobham and Andy Sumner for their invaluable contributions to my work on inequality. I am also thankful to many friends and colleagues, in particular to Javier Núñez and the great old gang of Cambridge PhD students for their contributions to my work on this subject. Over the years, Stephanie Blankenburg, Ha-Joon Chang, Mariana Chudnovsky, Camila Cosiña, Jonathan DiJohn, Jorge Fiori, Juliano Fiori, Daniel Hahn, Geoff Harcourt, Pamela Jervis, Mushtaq Khan, José Antonio Ocampo, Cristóbal Palma, Guillermo Paraje, Carlota Pérez, Jonathan Pincus, Ashwani Saith, Ignês Sodr , Bob Sutcliffe, Lance Taylor and Robert Wade also made important contributions. The usual caveats apply.

This paper is dedicated to Diego Armando Maradona, "El Pelusa", a symbol of our Latin American culture in all its glories and flaws —in its life-producing drives and its self-destructiveness (the subject matter of this paper is no exception).

Introduction

This paper studies the complex and intriguing issue of why the rich tend to stay rich, no matter what the rest of society throws at them. To do so, I return to the Ricardian tradition of understanding the distribution of income as the outcome of the political articulation of conflict between rentiers, capitalists, bureaucrats and labour —in which history, politics and institutions matter as much (if not more) than economic ‘fundamentals’. Also, in this tradition economic underperformance arises mostly from the shift in distribution from entrepreneurs to rentiers (from operating profits to rents). The focus of the analysis is on the persistence and change of institutions in Latin America’s recent past, in particular on the “iron law of oligarchies”, whereby dysfunctional institutions tend to rebuild (with Chile as a case study).

In the US, for example, as Acemoglu and Robinson (2006) describe, the traditional landed élites were able to sustain their political control of the South for at least a century after losing the Civil War by successfully blocking economic reforms that might have undermined their power, and by using their local political supremacy to disenfranchise blacks and re-exert control over the labour force. In Latin America, likewise, dysfunctional oligarchies have been remarkably effective at crafting their own re-creation after political shocks: so far, no matter what, they have been able to reengineer something resembling a “Southern-style” political settlement and distributional outcome.

The focal point of my analysis will be on how the Chilean élite has successfully transformed its “Southern-style” scenario into something approaching a ‘stationary process’ —in the sense that the unbalancing impact of shocks (such as the 1982 economic collapse, or the return to democracy in 1990) have had only limited life-spans. Although Latin America’s history is rife with shocks, its oligarchies have been able to landscape the new scenarios in such a way that they have been able to continue achieving their fairly immutable rent-seeking goals.

In the case of Chile, for example, they have done so mainly through three channels: one is by forcing straitjackets on new scenarios so as to restrict the scope of change —like when they imposed a draconian Constitution, Buchanan-style, and a series of *leyes de amarre* (or “handcuff laws”) on Chile’s young democracy, which included retaining Pinochet as head of the Armed Forces for another eight years, and then as a senator for life! The latter category was a group of pro-Pinochet appointees large enough so as to ensure the control of the Senate by right-wing parties no matter what happened at the elections. Another is by having the agility to reengineer their distributional strategies while maintaining their collective action so as to suit the new scenarios. And finally, by cleverly absorbing elements of opposing ideologies (such as now accepting the need for ‘social protection’), so as to keep their ideology hegemonic in the new scenario —according to Gramsci, any ideology with that aim must be able to do this. Their trump cards are ruthlessness in the first channel, and the capacity for solving any internal problem of ‘collective action’ and fancy footwork (or what Brazilians call “jogo de cintura e jeitinho”) in the other two.²

In distributional terms, the Latin American capitalist élite has (so far) managed successfully to stay always on top of the distributional conflict by following a complex distributional strategy which could be associated to what in game theory is known as a “Parrondo’s paradox” —or ‘a sequence of losing strategies that wins’.³ In its traditional formulation, this paradox consists of two games that are played in an alternating sequence. An analysis of each game in isolation shows them to be losing games *if played indefinitely* (i.e., they have a

² Or, as they say in golf, ‘It’s all in the hips’!

³ See Parrondo (1996).

negative expectation). However, when they are played in an alternating sequence, the resulting compound game is, paradoxically, a winning game. In other words, it is possible —as in Chile— to construct a winning strategy by playing apparently losing distributional games alternately.

It remains to be seen whether the Chilean oligarchy will succeed in doing this all over again vis-à-vis the impact of the massive political shocks of the social unrest of October 2019 and the pandemic. That is, whether they can successfully reengineer their distributional strategy for the fourth time since crashing the Popular Unity government in 1973 —this time, by trying to rebuild their Southern-style rule with their newfound European ‘new’ social democratic-style discourse.

Each of the previous three distributional strategies had a shelf-life, after which they had become counterproductive. Had the oligarchy continued to implement them, they would have become losing strategies. The secret of the oligarchy’s long-term distributional success has been making the switch on time.

If they succeed in doing this again, it will show that their Southern-style rule still remains a ‘stationary’ process —in terms of its capacity to absorb major shocks without altering its fundamental structure (i.e. by making their impact temporary). If not, it would mean that, in particular, the October 2019 social uprising was a shock too far for the oligarchy, one that finally had a more *permanent effect* on the rentier structure of oligarchy’s Southern-style rule. Namely, one that was able to reshape the Chilean political settlement and distributional outcome into something resembling a unit-root-style process, where the impact of shocks does not decay over time.

As my understanding of inequality steams from the Ricardian tradition of analysing inequality as the outcome of conflict —in which history, politics and institutions is what really matters— my analysis places the emphasis on Gramsci rather than Kuznets, on Hirschman rather than Solow, on Mazzucato, Amsden or Pérez rather than on neo-classical understandings of the relationship between technology and inequality. The focus is on self-construction rather than on fundamental forces of the universe. The key questions relate to issues such as what is it that helps in the formation of collective beliefs? How do spontaneous consensus types of hegemony emerge? How can they be changed? The accent is on ideology rather than technology; on agency rather than structure (provided that agencies are able to understand structure); on choice rather than (Piketty’s) historical ‘accidents’;⁴ and on political articulation rather than economic determinism. It is about fighting artificially created “distributional failures” ***in the sphere of production*** with Keynesian determination rather than surrendering market inequality to the likes of armchair rentiers, speculators (with more liquidity than imagination or morals), polluters, natural resource plunders and traders.

All these complexities make the analysis of inequality particularly difficult due to its intricacies and overdetermination —making our modest understanding

⁴ In Piketty’s original (and highly influential) work, there is no room for a ‘natural’ tendency for inequality to decline even when a country reaches economic maturity. In his neo-classical (and therefore necessarily mechanistic) model, increasing inequality is supposed to be intrinsic to a capitalist economy irrespective of its political settlement and level of development. (Piketty, 2014). For him, it took ‘accidents’ such as two world wars and a massive depression to disrupt this supposed pattern (for a discussion of this, see Palma, 2019a, Appendix 2). However, in his next (and outstanding) contribution (Piketty, 2020) he finally downplays the role of ‘accidents’ by switching his emphasis to ideology.

of its dynamics (despite recent progress) one of the most important analytical failings of current economic analysis.⁵

In fact, Krugman (2011) identified increasing inequality and Latin America's perennial economic underperformance as the two greatest analytical challenges in economics today. However, from my perspective the real challenge is to understand **the interaction** between the two in both mature and emerging economies —as high-income OECD countries are now almost infatuated Latin-style relentless inequality and perennial underperformance.

Basically, the high-income OECD now seems determined to mimic the (Ricardian-style) Latin American distributional process in which rentiers appropriate an ever increasing share of the national income, while capitalists get less and less via operating profits —forcing them to increasingly act as rentiers in their productive activities.⁶ This includes the key role now played by financialisation and intellectual property rights in non-financial corporations.⁷

The nature of the economic activates may have changed since Ricardo, but economic underperformance arising from shifts in distribution from operating profits to rents has not. It's Ricardo's growth model all over again! In fact, Ricardo (1817), himself a stockbroker who made most of his fortune as a result of speculation on the outcome of the Battle of Waterloo, argued that under certain conditions the above mentioned dynamic tends to dominate. One in which in the 'steady state' real wages end up being constant, capitalists make no profits and rents reach its maximum possible level. Only technological progress and international trade can come to the rescue and help reverse the slowdown in productivity growth resulting from this shift in distribution from profits to rents.

The specificity of Latin America's political settlements and distributional outcomes is not just about artificially constructed inequalities having come at the cost of economic performance, but how the region's dysfunctional oligarchies have shown a remarkable 'ability to persist' despite of the above, and in spite of economic shocks (such as the 1982 collapse, when Chile's GDP fell by no less than 20%, unemployment jumped to 30%, and half of the population dropped below the poverty line), and of political shocks (such as the return to democracy).

What has happened so far with the pandemic is yet another example of this phenomenon: while this plague devastates economic activity and living standards —undoing much of what had taken years to achieve in terms of reducing poverty and in some cases a bit of inequality—, most large fortunes have continued with their "perpetual mania".⁸

Latin America's fundamental political economy problem is that there are not many ways to reshape the structure of a 'system' with so little entropy: there are few ways one can redesign the structure of our society and economy —so it can move 'forward' in time—, if one can't change the fundamentals of its *status*

⁵ For some of the recent contributions, see Atkinson (2015); Bourguignon (2015); Galbraith (2016); Milanovic (2016, 2018, and 2019); Ocampo (2019); Palma (2011, 2016 and 2019a); Piketty (2014 and 2020); Scheidel (2017); and Taylor (2020).

⁶ Palma (2019b).

⁷ By 'financialisation', I understand the rise in size and dominance of the financial sector relative to the non-financial sector, as well as the diversification towards financial activities in non-financial corporations. Regarding intellectual property rights as currently implemented, they are counterproductive as they may well slow down (rather than speed up) the pace of innovation. As knowledge is a (global) public good, with no marginal costs associated with its use, restricting its access would *necessarily* cause market inefficiency. Furthermore, as knowledge is the main input for the creation of further knowledge, restricting its use inevitably leads to an oligopolistic market for knowledge. The need to provide incentives to innovate is one thing; artificially restricting access to knowledge is quite another (see Stiglitz, 2007; and Palma, 2019a).

⁸ Palma (2020a).

quo: that those at the top can continue to appropriate such an absurd share of national income, while doing the 'low hanging fruit'-type of activities they favour. In Darwinian language, as evolution inevitably creates uncertainties to dominant agents, the main problem with such a 'system' is that the oligarchy expends so much energy in trying to 'stop time' that there is little left for moving the system forward.

There are many underlying questions: does Latin America's huge inequality reflect a variety of 'fundamentals' or specific interactions between power structures and choice? Is high market inequality the product of somehow 'exogenous' factors (as in ' $r > g$ ' of Piketty's early neo-classical models) or of complex interactions between political settlements and market failures (as studied in Palma, 2019a)? How do we get through the veils obscuring these interactions and distorting our vision of the often self-constructed nature of inequality? Has neo-liberal globalisation-cum-financialisation broadened the scope for "distributional failures"?

One key analytical hypothesis proposed here is that Latin America's experience shows that rather than thinking, as in neo-classical terms, of the possible **concrete effects** that well-known factors may have on inequality (e.g., technology or education), it would be more illuminating to try to understand the **concrete expressions** that these factors may find in inequality. Some of the pieces of the distributional puzzle may well be the same in different experiences of inequality, but the way they fit together may well differ —sometimes significantly.

In the case of education, for example, there is little doubt that it can have a significant distributional impact. However, the particularly low income-share of Chile's upper-middle (deciles 7 to 9, 35% of national income) is identical to those of Malawi, Central African Republic, and Burkina Faso even though in Chile gross tertiary enrolment rate reaches almost 90% while in the other countries it does not even get to double digits. In fact, Burundi, DR Congo, Niger, Madagascar, Mauritania, Angola and Cote d'Ivoire, also with an enrolment-rate in single digits, have an income-share for this group which is actually higher than Chile's. The issue, of course, is not whether education impacts the value of marginal productivities (it certainly does), it is about its quality and **who appropriates** that additional output! With the topic of the growing inability of labour to get the value of its marginal social contributions (due to a lack of property rights over its energy and skills), being of paramount importance.⁹

In other words, **the specificity** of Latin America's inequality stems from the particular ways in which distributional struggles between rentiers, capitalists, bureaucrats and workers have manifested themselves there, the different strategies that oligarchies have adopted to face and temporarily overcome these struggles (the main subject matter of this paper), how the capitalist class has increasingly joined the ranks of the rentier class (the main subject of Palma, 2019b), and how further distributional challenges have been created by this process, and so on.

Oddly enough, some still continue to blame Latin America's inequality on colonial institutions from half a millennium ago such as *mita* (mandatory public service by the indigenous population) and the *encomienda* system that rewarded conquerors with the labour of conquered people.¹⁰ Others, as in many neo-classical narratives —somehow resembling nineteenth century Newtonian physics (i.e., methodologies of mechanical determinism and simple causalities)— look at the subject with tunnel vision, overstating single issues (such as education or

⁹ This also distorts incentives to acquire skills: what would be the point of making the effort if the additional output is bound to be appropriated by others? (See Pagano, 1997).

¹⁰ For Williamson (2009) —quite rightly— the supposed monotonous persistence of Latin America's inequality is just a myth.

skill-biased technological change).¹¹ While others go as far as blaming the ‘lack of major wars’, or any such historical ‘accidents’.¹²

Indeed, many people’s monotonous insistence on blaming Latin America’s huge inequality on traditional ‘exogenous’ or crude path-dependency factors is akin to using a pair of scissors to cut an analytical knot they are unable to untie.

In turn, it is unfortunate that Piketty, in his first and more influential book (2014), by unnecessarily relying on the neoclassical theory of factor shares, led the debate over increased inequality in most OECD countries since Reagan and Thatcher, and the fall of that wall, in the wrong analytical direction —like the head of a hunt leading the pack down the wrong path. Basically, in his neoclassical theory, if one has *too much of a good thing* —in fact, in his analysis two good things: too much investment and too high an elasticity of substitution (production flexibilities)—, one unfortunately ends up having higher inequality. It would be hard to put a better spin on increasing inequality than this neo-classical one.¹³

Instead, as Stiglitz (2012) and I have argued (Palma 2011, 2016 and 2019a), inequality **is a choice**; and as I insist in my work, nothing reveals more transparently **who we truly are** than the inequality we collectively choose to construct. As Sartre has argued, *we are our choices*.¹⁴ The bottom line, as the title of my 2016 paper indicates, is that **every country deserves the inequality it has**. It is just not credible to continue claiming that we are innocent bystanders of supposedly exogenous fundamentals.¹⁵

In other words, one must always reject mechanical determinisms and simple causalities and insist on our ultimate freedom and responsibility. “I am my freedom”, says a character in one of Sartre’s plays. Every act is a self-defining one, and no act can really be blamed on so called ‘external’ factors. The classic quotation on this matter comes from Shakespeare, a speech in *King Lear*:

This is the excellent foppery of the world, that, when we are sick in fortune, —often the surfeit of our own behaviour—, we make guilty of our disasters the sun, the moon, and the stars: as if we were villains by necessity; fools by heavenly compulsion; knaves, thieves, and treachers, by spherical predominance; drunkards, liars, and adulterers, by an enforced obedience of planetary influence; and all that

¹¹ Most neoclassical analyses of Latin America’s inequality crucially fail to explain why it is much higher than in many middle-income countries elsewhere, for example, in Asia, North Africa, the former Soviet Union and Eastern Europe (among others), even though some of the issues they highlight apparently point in the opposite direction. For example, the latter often have even more market failures and rigidities than Latin America; they have prices, institutions and social capital that are even less ‘right’; they have property rights over physical and intellectual assets that are less well-defined and less well-enforced; they have educational systems that are even more segmented, with the poor often getting an even more dismal deal; they discriminate on gender and race even more than in Latin America; they have even greater shortages of skilled labour; their democracies are even more ‘low intensity’, and with more problems of ‘governance’; they have an even greater dependence on political connections and corruption to achieve success in business. But, despite all of this, these countries are less unequal than Latin America (sometimes significantly so).

¹² Scheidel (2018); and Piketty (2014).

¹³ For a critique of Piketty’s neo-classical analysis, see Rowthorn, (2014); Taylor (2014 and 2019); Harcourt (2015); and Palma (2019a, especially Appendix 2).

¹⁴ Sartre (2004).

¹⁵ Kaldor (1956), in his analysis of the instability issue of the Harrod–Domar model, was the first to break the neo-classical mechanistic spell on the determinants of inequality —prompting Solow’s wrath, as he argued that it was impossible to think of an efficient distribution of income that was not automatically determined by the value of marginal productivities (Solow, 1956).

we are evil in, by a divine thrusting on: an admirable evasion of whoremaster man, to lay his goatish disposition to the charge of a star!.¹⁶

At least it does seem finally to be becoming “common sense” (in Gramsci’s perspective) that the ever-increasing market inequality that has characterized the global landscape since Reagan and Thatcher has been ***an artificially constructed distributional failure***. Warren Buffett famously explains this clearly and succinctly: “There’s class warfare, all right, but it’s my class, the rich class, that’s making war, and we’re winning”. Fundamentals? What fundamentals?

Basically, if Smith’s ‘invisible hand’ existed, and was what guided behaviour, this relentless increase in inequality (particularly in market inequality; i.e. before taxes and transferences; see Appendix 2) could not have taken place, as market ‘compulsions’ would have put a stop to it —and to its artificially ‘tailor-made’ foundations. In fact, it feels almost ridiculous even having to state that ever-increasing market inequality has been an artificially constructed distributional failure; it’s like somebody at the circus pointing out that when the magician saws a woman in half, it’s only a trick!

1.- Some background issues

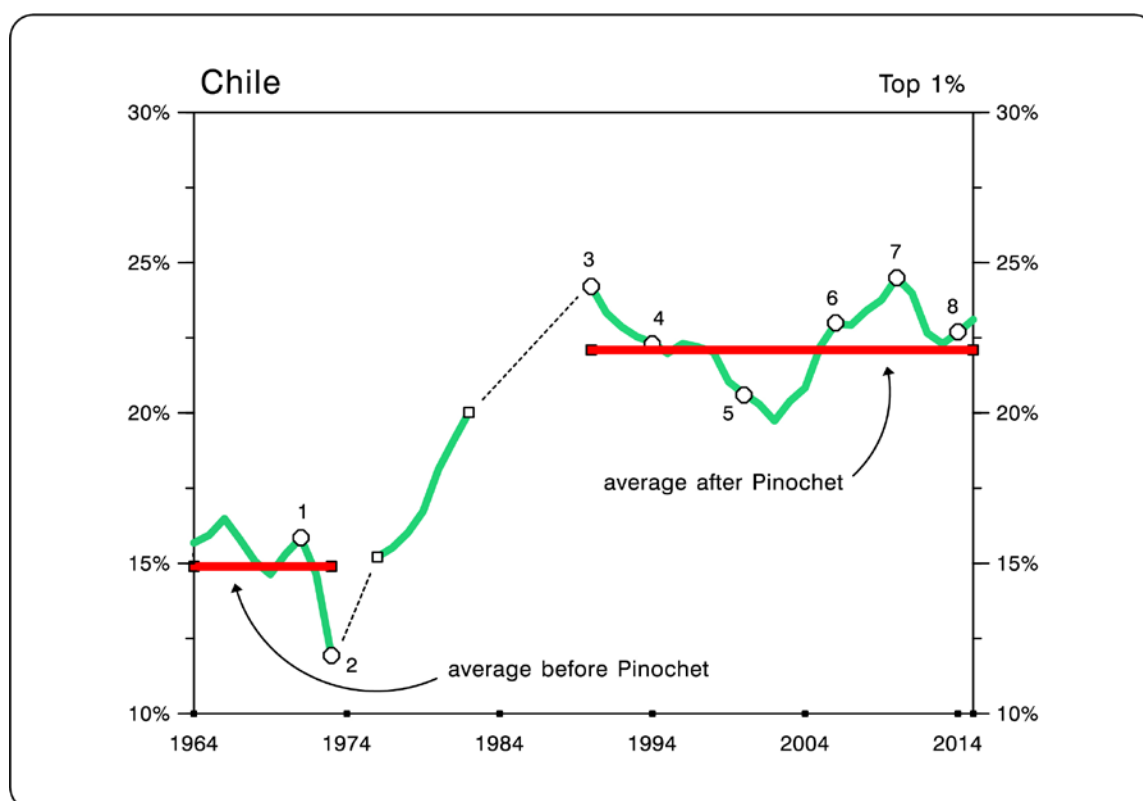
1.1.- ‘Ratchet effects’

One of the issues I shall analyse in this paper (mostly ignored so far in the literature), which has proved to be an important distributional stylised fact in post-war Latin America, is the “distributional-ratchet” effect resulting from the fact that improvements in inequality have tended to be short-lived, while deteriorations have more permanent effects. That is, the well-known difficulties in human history for the reversal of social dynamics seem to apply asymmetrically to inequality: increases are hard to reverse while improvements are particularly fragile. What happened in Chile during Allende’s short presidency (and its decline in inequality) vs. with Pinochet’s massive deterioration clearly indicates this, creating a long-term upward ratchet at the top of the income scale (Figure 1).

¹⁶ Edmund, Act 1, Scene 2 (132): www.online-literature.com/shakespeare/kinglear/3/

FIGURE 1

Chile: share of pre-tax income of the top 1%, and the upwards “ratchet effect” left by the dictatorship as its distributional legacy, 1964–15



• **1**=election of Allende; **2**=Pinochet's *coup d'état*; **3**=the year Pinochet had to call a plebiscite seeking a mandate to remain in power for another eight years, and first democratic government (centre-left coalition, the 'Concertación') after Pinochet lost his plebiscite; **4**, **5** and **6**=next three centre-left governments; **7**=election of a centre-right government; and **8**=the centre-left returns to government. Averages are harmonic means (1957-73, and 1990-2015).¹⁷ 3-year moving averages.

• *Source*: WID (2020), based on Atria et al. (2018).¹⁸

What is most striking is that this ratchet at the top occurred despite the fact that Pinochet and its allies lost his plebiscite badly, and that in the post-return-to-democracy period, there were four consecutive 'centre-left' governments, and all with a political coalition that even included President Allende's Socialist Party.

Standing out among other regional distributional ratchets is the case of Brazil. The Brazilian oligarchy was not only able to sustain the increase in inequality brought about by the 1964 *coup de état*, but it also managed to carry on enjoying these gains long after the return to democracy—in fact, until the election of President Lula da Silva (see Figure 2).¹⁹ This remarkable persistence of high inequality (subject only to minor improvements at best) also applies to other countries of the region.

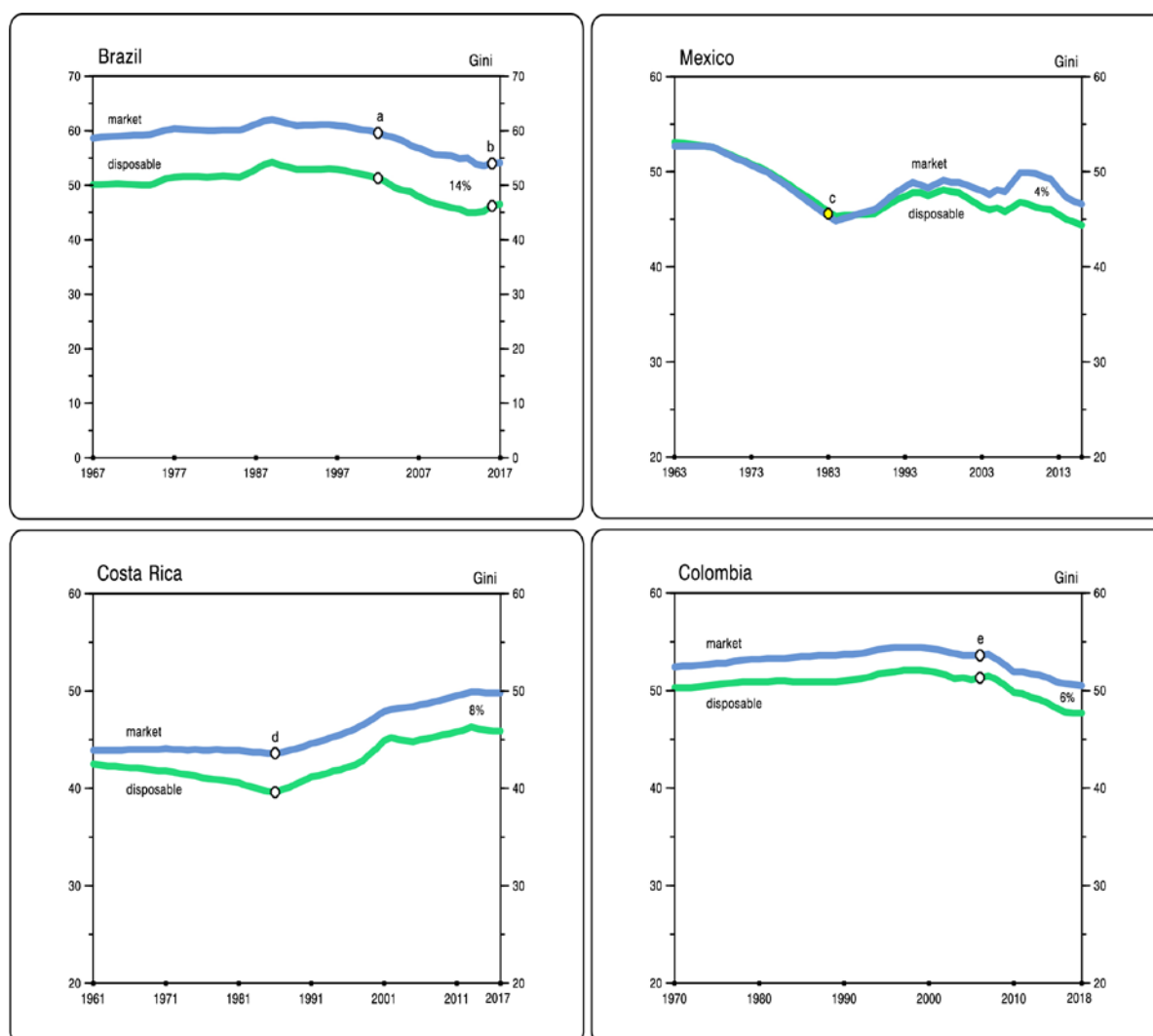
¹⁷ For the non-specialist, the harmonic mean is one of the three Pythagorean means. It is more appropriate for the average of ratios as it mitigates the impact of outliers; it also contains more information than the median. It is the reciprocal of the arithmetic mean of the reciprocals.

¹⁸ Broken lines refer to years for which there are no data. As in the source, 'fiscal income' from 1964 to 1981, and 'pre-tax national income' from 1990 onwards.

¹⁹ On the rapid deterioration of inequality in Brazil after the 1964 *coup*, see Fishlow (1972).

FIGURE 2

Colombia, Costa Rica Brazil and Mexico: market and disposable-income Gini, 1960–2017



• a=election of Luiz Inácio Lula da Silva; and b=parliamentary *coup d'état* against Dilma Rousseff; c=election of Miguel de la Madrid; d=election of Óscar Arias; and e=re-election of Álvaro Uribe. Percentages shown in the panels indicate the relative reduction of the market-Gini (via taxes and transferences).

• Source: WIID (2020); and Palma (2019a).

Moreover, as the figure indicates, countries of the region barely reach double figures when it comes to improving their 'market' inequality via taxes and transferences. These efforts are minimal compared to those of European countries (all the way up to 50%; see Appendix 2) —and even to that of Trump's US (25%)! How did Latin America manage to achieve so little despite so much 'progressive' talk?

And Brazil's 14% reduction in its market-Gini, like South Africa's similar figure, is a particularly modest effort, since fiscal revenues (as a share of GDP) in both countries are relatively similar to the OECD.²⁰ The difference between them, of course, is that South Africa, despite relatively progressive taxation, fails to achieve more due to an ineffective system of transfers to the poor. Brazil, by

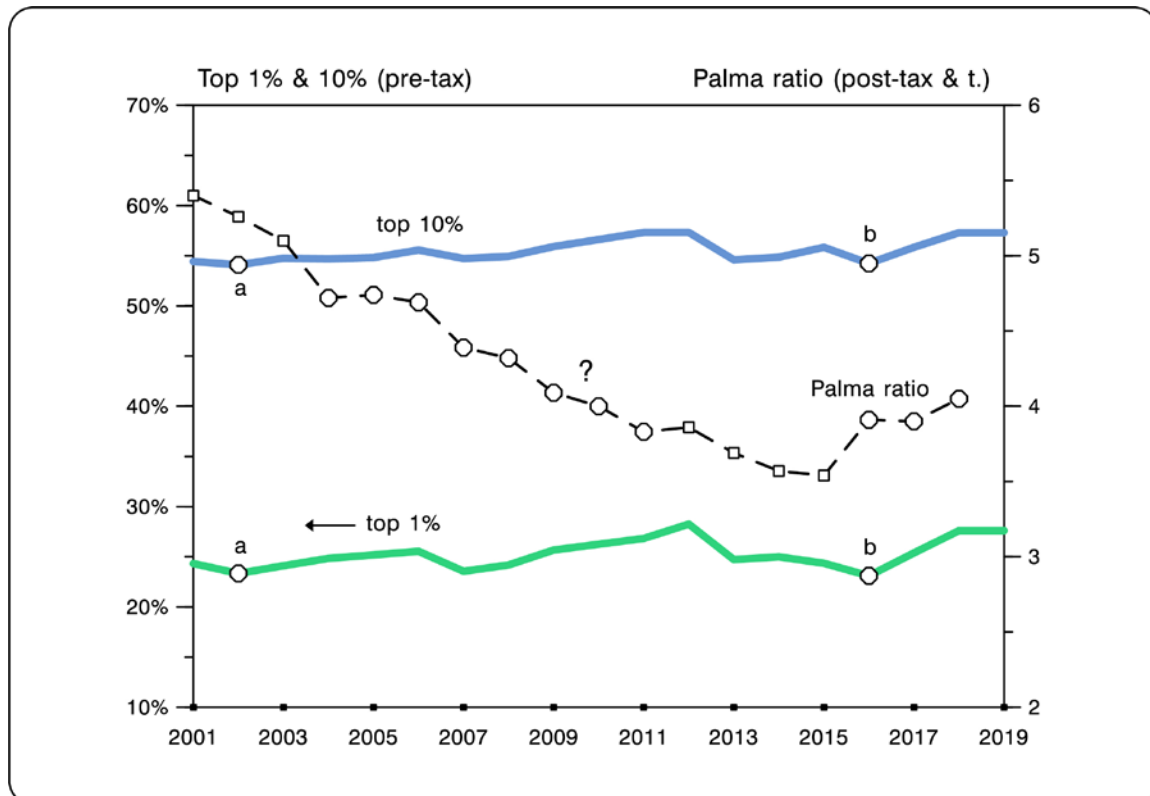
²⁰ Di John (2006); Lieberman (2003); and OECD (2020a).

contrast, although it has (or should I now say it *had?*) a more effective programme of transfers, falls down badly on its highly regressive tax structure.

Indeed, another source (WID, 2020), even calls into question Brazil's relative improvement in inequality (as shown in household surveys) during the four successive governments of the PT (Partido dos Trabalhadores, or The 'Workers' Party'). It seems that the Brazilian inequalising 'ratchet' has really continued unyielding until today! (Figure 3.)

FIGURE 3

Brazil: pre-tax shares of income of the top 1% and top 10%, and post-tax and transference Palma ratio, 2001-2019



• **a**=election of President Luiz Inácio Lula da Silva; and **b**=parliamentary *coup* against President Dilma Rousseff.

• Source: WID (2020) for income-shares of the top 1% and 10% based on De la Rosa (2020); and World Bank (2020) for the Palma ratio.

There's little indication here that the supposed minor decline of the income share of those at the top during the PT era did actually take place (other than on paper). As ex-President Cardoso famously said, "Lula knows how to please the *élite*".²¹ Even successful policies during the PT period, such as for poverty reduction, for the formalisation of labour contracts, and for the increase of the minimum wage (as well as for slowing-down the destruction of the Amazon) are now at risk not just because of the economic impact of the pandemic, but also due to its current "peripheral-fascist" ideology, its negationist politics on pandemics, its petty

²¹ <https://politica.estadao.com.br/noticias/geral,fhc-na-hora-de-governar-lula-sabe-como-agradar-a-elite,108576>

Amazonian-nationalism, and early Washington Consensus/Chicago-style neo-liberalism in economic policies.²²

The same scepticism is called for Chile's much-heralded minor improvements on inequality (see Figure 1 above and 9 below). For those 'progressives' in Latin America wanting to change the "Southern-style" distributional equilibrium, it has proved much easier to 'talk the talk' than 'walk the walk'!

1.2.- How dysfunctional institutions are rather effective at their own re-creation when shocked out of balance

As suggested above, all this brings us back to the complex issue of 'persistence and change in institutions', and in particular how dysfunctional institutions are so effective at recreating themselves —as the landed élite did in the South after losing the Civil War. Likewise, the Chilean oligarchy was able to do the same, despite losing badly the 1988 plebiscite and then four presidential and parliamentary elections thereafter. As times have changed, rather than lynching their object of hate, it's now more effective to co-opt them. However, as times have not changed *that* much, the oligarchy managed to impose on the majority a straitjacket Constitution, littered with institutions above democratic control. In turn, thanks to supramajorities being required in Parliament, and to the 'appointed' life Senators, those institutions above democratic control made changing the Constitution practically impossible. It took a social explosion of the magnitude of that of October 2019 to shock Chile's "Southern equilibrium" out of balance enough to force business leaders to convince the powers that be to start constitutional change. When the referendum on this possibility took place exactly a year after the social unrest (and 30 years after the return to democracy), it attracted an 80% positive response (on a high turnout)!

As to the role played by the 'new' left in helping sustain Chile's "Southern equilibrium" (see Appendix 1), according to Gramsci, any ideology that wants to remain hegemonic must be able to absorb elements of opposing ideologies; but it must do so in an *imaginative way*, articulating them with the essence of its own ideology. That is, for a consensus to remain hegemonic, dominant groups have to make ideological concessions to subordinate groups, but without endangering their domination. This was what the centre-left parties did so badly after the 1988 Plebiscite, while the right-wing forces did so well after their bad defeat, helping the business élite to retain *de facto* political power. The centre-left parties, meanwhile, inspired by the "Third Way" of the Western European 'new' social democracy, made that Gramscian ideological integrative effort in a lazy, often opportunistic way, letting the new neo-liberal economic ideology simply replace its previous ('post-war-type') social democratic ideology.

Here the similarities to what happened in South Africa (Africa's honorary Latin American country) after the beginning of democracy in 1994, is also more than superficial: the battle lost by the Afrikaner political élite may be as big as they come, but the white capitalist élite (helped by the co-option of a critical mass of the ANC élite) is still appropriating the highest share of income in the world today!²³

²² In terms of the current pandemics, if we continue to destroy habitats and ruin ecosystems, other viruses will be waiting to jump from animals to humans; it's likely that the continued destruction of the Amazon is the next health crisis awaiting its big break. At the moment of writing, even areas outside the Amazon, such as Pantanal, are now being burnt to the ground —more than a quarter of it has already been destroyed. As Einstein once said, "Two things are infinite: the universe and human stupidity" (adding, "although I'm not sure about the universe").

²³ Palma (2011, Appendix 3).

From this perspective, as Acemoglu and Robinson (2006) point out, one should never lose sight of the distinction between the two components of political power, the *de jure* (institutional) and *de facto* political power. Latin America's political misfortune is that the oligarchy's *de facto* political power is such that dysfunctional institutions have been able to survive democratic 'shocks' relatively unscathed. The Latin American 'new' left has proved to be just one casualty in that history (see Appendix 1).

1.3.- Inequality as an anti-coordination 'chicken game'

In game theory, a 'chicken game' is a model of conflict associated with a diverse range of social conflicts. It's a question of which player yields first, as in the 1955 film *Rebel Without a Cause*; stolen cars are raced towards an abyss, and whoever jumps out first will be deemed a 'chicken'. Bertrand Russell (1959) also famously used it as a metaphor for the psychotically dangerous game of nuclear brinkmanship.

This is an 'anti-coordination' game because the shared resource is rivalrous (although non-excludable). Namely, sharing comes at a cost; i.e., it is subject to a negative externality. This, of course, does not have to be the case in distributional games if the players are involved in a Marshallian 'efficiency wage' scenario because of the positive feedback between wages and productivity growth. However, try explaining that to a neo-liberal oligarchy whose income depends on their not understanding.

The unstable state of affairs that characterises a game of chicken (sometimes also called a 'hawk/dove' game) leads to a situation in which there are only two possible (and opposite) Nash equilibria —corresponding to each player's preferred strategy.²⁴ Anything in between is an unstable mixed outcome, always subject to being challenged. So one effective tactic (particularly relevant for this story) would be for one party to signal his or her intentions convincingly enough —in other words, it could easily become a game of 'brinkmanship': a strategic move designed to avert the possibility of the opponent switching to aggressive behaviour. This is one reason why ***an 'irrational' player tends to have the upper hand***. And since credible threats —no matter how irrational— can be very effective, the set of institutions and rules within which a distributional struggle is played out becomes crucial as it helps promote the credibility of one or another party.

In fact, one way of understanding the post-1980 neo-liberal transformations is in terms of the creation of an ***artificially constructed*** institutional scenario where the brinkmanship of the top —irrational though it may be— should be taken extremely seriously by workers and the state. It now seems clear that these reforms had little to do (in both mature and emerging economies) with increased efficiency, and a lot to do with helping capital to regain its legitimacy and recover the upper hand —a legitimacy it had lost in the depths of the 1930s to Roosevelt's determination in implementing the institutional transformation of the *New Deal*, the horror of war, the increasing organisation of the working class, and the genius of Keynes. Even in the US, the income of the

²⁴ In this game, the strategic space for both players would be 'demand redistribution' and 'not demand redistribution' for the majority player, and 'yield to redistribution' and 'not yield to redistribution' for the capitalist elite. This is a multiple equilibria story. In turn, the Nash equilibria would be 'demand redistribution', 'yield to redistribution', and 'do not demand redistribution', 'do not yield to redistribution' for the majority player and elite player, respectively. In the first, the majority player has the upper hand, while in the second it is the elite one.

bottom 40% grew faster than that of the richest 1% during the three decades from the end of the war until Reagan.²⁵

One of the aims of the 1980s reforms was to reverse this. From Walter Benjamin's perspective (1966), all class society is in a permanent state of emergency because rulers are always under threat;²⁶ so neo-liberalism aimed at building a consensus and a praxis —and a "common sense"— that would help to create a class society in which rulers escape this threat by their ability **to debilitate** the rest of society enough by imposing on them a continuously insecure life. In this scenario, a mobile and malleable agent might achieve an unrivalled dominance. In the jungle, big capital (especially a rentier financial one) is king! And in this context, any progressive nationalist development agenda runs the risk of becoming a collective suicide pact.

This brings to mind Foucault's (2004) proposition that neo-liberalism is not really a set of economic policies but a new, more effective *technology of power*.²⁷ So workers are now back to old-fashioned precarious jobs; safety nets are being deliberately made increasingly porous; and easy access to persecutory debt is leading to what Krugman (2005) calls "the return to a debt-peonage society". Surely, what Thatcher had in mind was not so much a property-owning democracy as a 'mortgage-owning' one! In turn, 'subsidiary states' allow little or no space for policy options or agencies, other than those that are meant to keep capital sweet.

And the uncertainties of a new technological paradigm have not helped either, giving massive opportunities to financial capital and a few particular skills and innovators, while bringing further uncertainties to the majority of workers and the state.²⁸

The bottom line for neo-liberalism is how to reconstruct an economic and institutional scenario in which everybody knows that capital can pull the plug whenever it wants to. Under these circumstances, the ideological acceptance by the majority of the "preferred" strategy of the rich could be considered 'smart', rather than 'chicken', making such an unfavourable position more bearable. Shared pain can even feel reassuring. After all, as Benjamin also reminds us, before all philosophy comes the struggle for material existence.

In developing countries, the challenge for capital to develop more effective forms of legitimacy, and more sophisticated technologies of dispossession, has been even greater. In the new complexities of a post-Cold War scenario, just having a minor Mussolini or two, such as Pinochet, was no longer enough.

The neo-liberal discourse may have burst onto the world stage during the thirst for new ideas in the 1970s, promoting 'order', market efficiency, individual initiative, non-paternalism, sound macroeconomics and a new concept of the state. However, what was ultimately on offer for workers and the state was a permanent life on the edge and a high-risk and unstable 'order' in which only mobile capital can really thrive, with the state mostly reduced to a 'fire-fighting' role.

In a way, Keynes' ideas were mostly about fighting these types of inefficient and old-fashioned 'anti-coordination' games, searching for more efficient and stable cooperative outcomes. The 'mass production for mass consumption' technological paradigm also helped this type of scenario, especially as it was in its 'mature stage'.²⁹ However, if capital or labour pushed things towards brinkmanship scenarios, what was imperative for Keynes was to prevent

²⁵ Saez and Zucman (2016); and Palma (2019a).

²⁶ On 'states of emergency', see Arantes (2007).

²⁷ Frangie (2008); Palma (2014).

²⁸ Pérez (2002).

²⁹ Mazzucato (2013 and 2018; Pérez (2002).

a player prone to 'irrational' behaviour —such as financial capital— from getting the upper hand.

2.- Why the rich remain rich: on the Chilean capitalist élite "ability to persist"

As already suggested, one possible explanation of Chile's stubbornly stable inequalising scenario is that it somehow resembles a 'Parrondo's paradox': it has been possible to construct a winning strategy by playing losing games alternately, switching between them when the game could become counterproductive (when it has passed its 'sell-by' date).

There are many examples of these counter-intuitive reversals; in financial markets, for example, one can think of games that would guarantee that a player would lose all his money, but could generate a winning streak if played alternately.³⁰

In the case of Chile, this specific political scenario is rather transparent — although the oligarchy's 'winning strategy' has involved more than two games, so its mathematical solution would imply a more complex convex scenario than the usual linear combination of two games.³¹

The basic political dilemma for any oligarchy determined to hold on to such degrees of inequality is how to construct a winning strategy that is sustainable **when in a democracy**, given the fact that the oligarchy forms such a tiny minority and that the distributional outcome that it seeks is so remarkably unequal.

What is needed to build a long term winning strategy of this type is the power to narrow down the range for change (by imposing constitutional and legal limits to it), and both the flexibility to switch between strategies as soon as they become counterproductive, and the capacity to solve any internal 'collective action' problem that may emerge along the way in order to ensure cohesion —so that members act together (even when individuals may have incentives to free-ride), a phenomenon that is sometimes associated with the concept of "élite closure".³² In fact, the role of the élite's capacity for collective action in helping them to get the upper hand is a subject which was already highlighted in Adam Smith's masterpiece; discussing the institutional and political scenario in which wages are settled, he says:

It is not, however, difficult to foresee which of the two parties [capitalist or workers] must, upon all ordinary occasions, have the advantage in the dispute, and force the other into a compliance with their terms. The masters, ... can combine much more easily; and the law, besides, [is on their side] (Smith 1776, Book 1, Chapter 5)

These are crucial components for the oligarchy's **ability to persist**. From this perspective, Douglas North was surely right when he developed his 'limited access order' hypothesis: how political elites able to maintain cohesion can divide up the control of rents and block the access of others.³³

³⁰ See, for example, <http://www.nytimes.com/2000/01/25/science/paradox-in-game-theory-losing-strategy-that-wins.html>

³¹ For an example of a 3-periodic game, see Key, et al, 2002.

³² In the recent plebiscite to change the Pinochet's Constitution, which got 80% national support, only in the three upper class districts of Santiago there was a majority against.

³³ North et al. (2007).

3.- 'Strategy 1': how to convert the probabilistic outcome of a distributional chicken-game into a deterministic 'winner-takes-all' scenario using terror

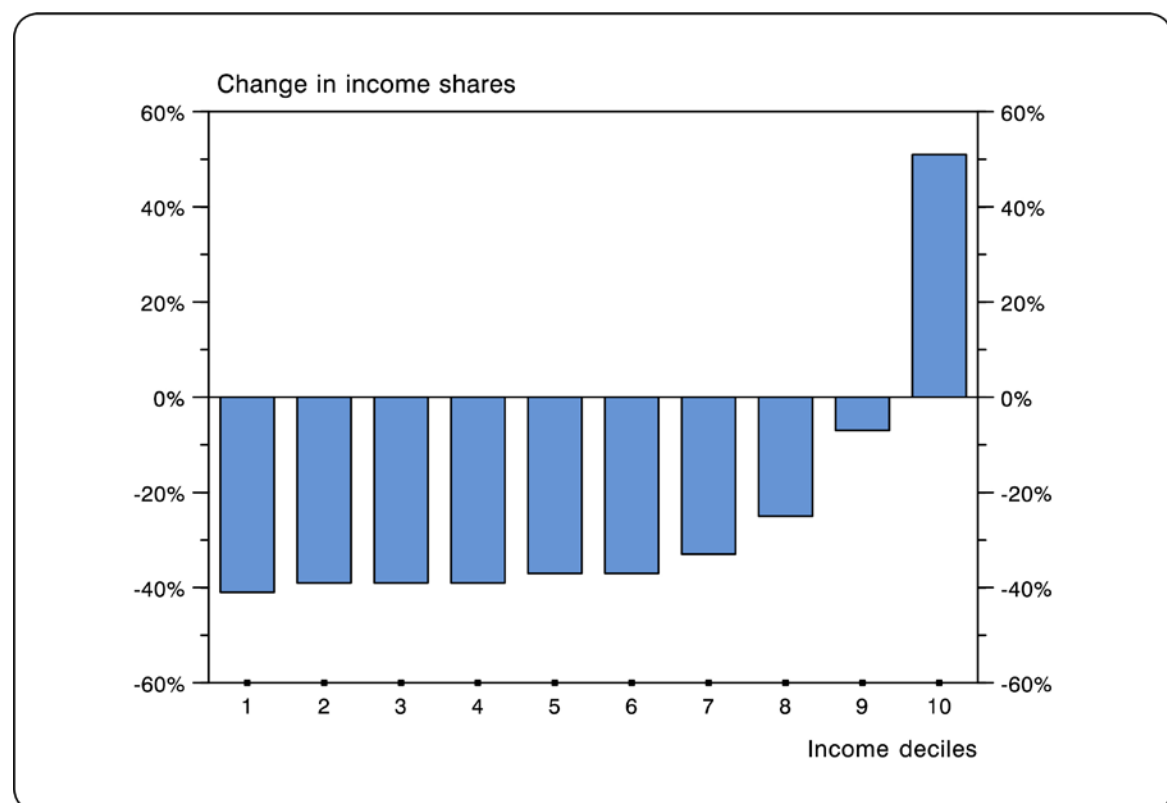
When Chile elected a left-wing government in 1970 —and that government (unusually enough) was prepared to implement the radical distributional programme for which it had been democratically elected (see Figure 1 above, and 5 and 6 below)— the Chilean oligarchy switched to the nuclear option of a *coup de état* (in a country with a long democratic tradition).

In game theory language, the oligarchy succeeded in switching the traditional 'game of chicken' distributional scenario from one in which the poor were getting the upper, to one in which it could implement its own "preferred" distributional strategy unimpeded —i.e., a 'winner takes all' scenario. The key component of this new "Nash equilibrium", with its particularly asymmetric set of distributive strategic choices, and the corresponding payoffs, was that the all-too-powerful top income player could now easily convince the majority that there was no point in trying to challenge this scenario while it had the whole apparatus of state terror at its disposal.

The distributional outcome of this new 'insatiable appetite' distributional strategy —the oligarchy's 'strategy 1' in this narrative— is evident in Figure 4.

FIGURE 4

Chile: changes in income shares between 1973 and 1987



• **Source:** calculations done by Pamela Jervis and the author using the FACEA (2019) database.³⁴ Data refer to household per capita (pc) income in 'Greater Santiago' (where

³⁴ In Chile, there are two household surveys. One is this, and the other is a national one (CASEN), which started in 1987, and is carried out every two or three years (see <http://www.mideplan.cl/casen>). The data in WB (2020) and SEDLAC (2020) correspond to the latter survey.

about 40% of the population lives). It excludes from family incomes those of lodgers and domestic servants living in the house, those declared as 'zero', 'does not know', and 'does not answer'.

In fact, the share of D10 increased from 34% of national income to no less than 52% during this fourteen-year period (1973-1987) —for which even the share of D9 had to be squeezed! This scenario resembles a reverse Robin Hood who not only robs the poor to give to the rich, but also robs the rich to give to the very rich!

4.- 'Strategy 2'. The new challenge for the élite: how to reconstruct a more sophisticated form of legitimacy via a more refined technology of power.

No matter how vicious the dictatorship might be, the oligarchy would not be able to play its 'strategy 1' indefinitely. Inevitably, towards the end of the 1980s, the distributional game began to move away from its (terror-based) Nash 'equilibrium' as new generations began to lose their fear of challenging the political settlement and distributional outcome associated with the oligarchy's 'preferred' strategy.

The only way out of this conundrum was for Pinochet to try to legitimise his rule by calling a plebiscite in 1988 that would allow him to remain as Head of State for another 8 years —one that he lost badly, even though the previous year he had tried to reverse some of the worse aspects of his distributional policy (see movement from 3 to 4 in Figure 7 below).

In fact, as he tried to improve his 'democratic credentials', he shot himself in the foot badly: just weeks before the plebiscite, he signed the UN Convention on Human Rights, an action he would live to regret as it was his ratification of this convention that allowed Juez Garzón from Spain to ask the British government for his extradition in 1998. This was the first time that a former head of government was arrested on the principle of 'universal jurisdiction'. Also, and again for the first time, this led to the principle of the immunity of Head of States (or former ones) not applying to crimes against humanity being enshrined in international law.

As Pinochet lost his plebiscite, and his supporters also lost the subsequent presidential and parliamentary elections badly, the élite had little choice but to switch its distributional strategy (to 'strategy 2'). This they did rather effectively.

Essentially, this 'strategy 2' resembled the ancient Roman Catholic practice of buying 'indulgences', by which sinners (in this case the oligarchy misbehaving during the dictatorship) could pay for certificates that recognised that their penance had washed them free of sin.

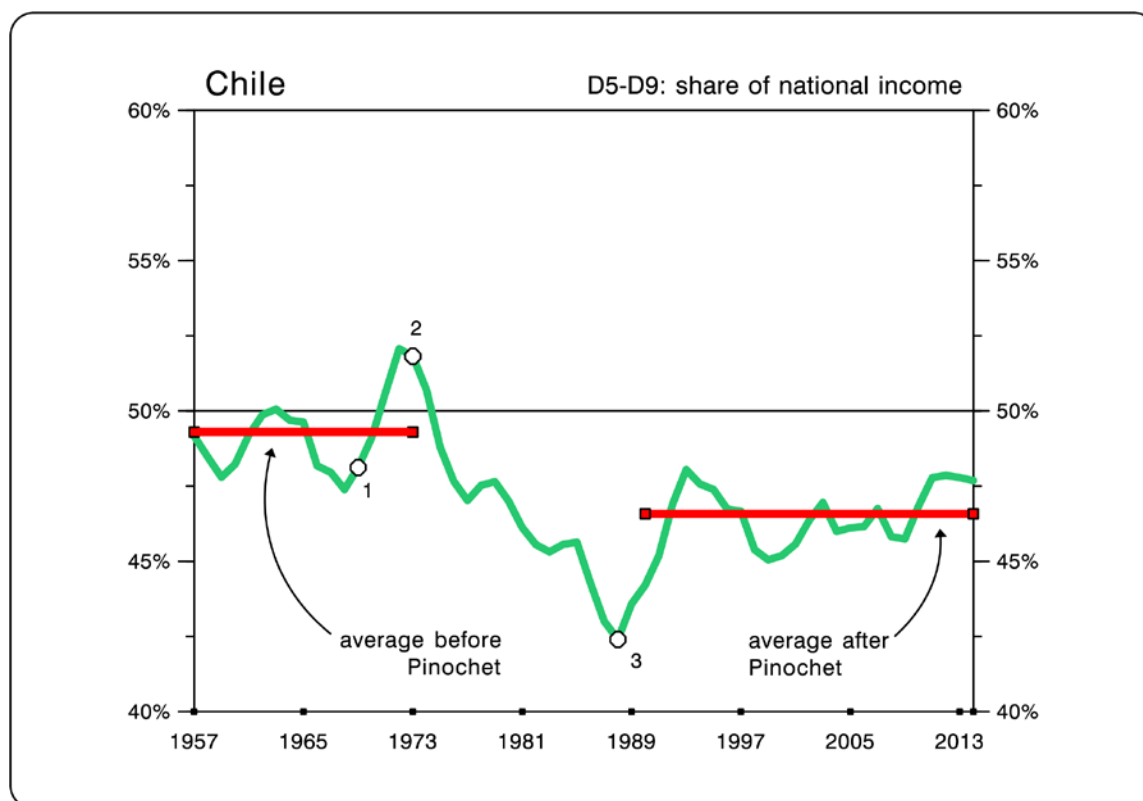
Suddenly, those at the top became 'born-again democrats', even supporting some progressive distributional policies of the new centre-left democratic government. They even turned out to be in favour of more progressive tax reform, although (with the help of 'life Senators' appointed by Pinochet) they succeeded in imposing the condition that this would be only a temporary measure. They also supported an increase in the minimum wage and other policies for poverty reduction, a mild reform of labour legislation, and so on.

A crucial component of 'strategy 2' was the need for the oligarchy to rebuild its traditional distributional alliance with the middle and upper-middle since, as Figures 4 above and 5 below indicate, they too had been squeezed during the top's 'winner-takes-all' distributional strategy. Therefore, it also supported (and pressured) the centre-left government towards different measures to benefit this sector. So, the share of deciles 5 to 9 recovered some of the ground it had lost during the dictatorship, but then stabilised at a level

below 50% of the national income —well below what it had enjoyed before 1973, indicating a downward ratchet for the middle and upper-middle. (Figure 5.)

FIGURE 5

Chile: share of income of the middle and upper-middle (D5-D9), 1957-2014



• **1**=election of President Allende; **2**=Pinochet's *coup d'état*; **3**=election in 1989 of the first of four consecutive centre-left governments after Pinochet lost his 1988 plebiscite; after **3**=next three centre-left governments and one right-wing one.³⁵ Averages are harmonic means (1957-73, and 1990-2014). 3-year moving averages.

• *Source*: as in Figure 4.

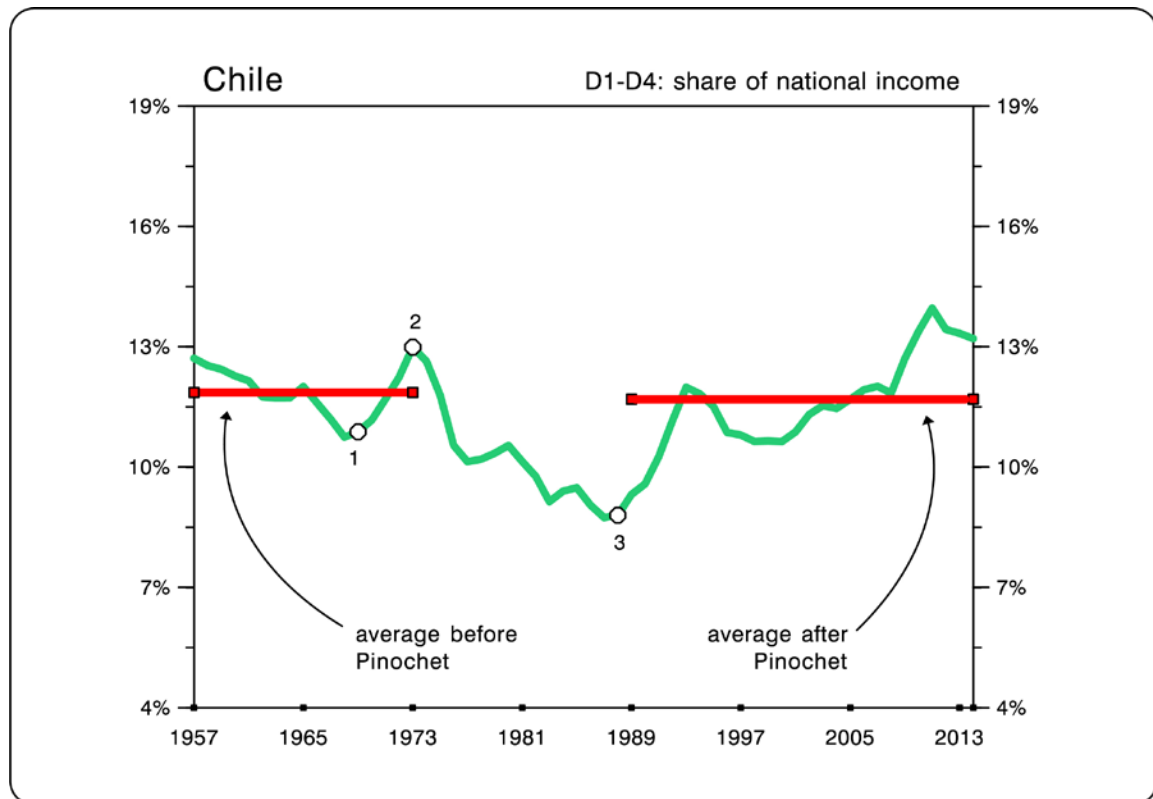
The key message of this figure is that Chile is one of the very few countries in the world where deciles 5 to 9 are unable to defend their half of national income (Palma, 2019a). Also, this picture does not really fit within a 'public choice' perspective where the process of rational decision making favours logic, objectivity, and analysis over subjectivity and intuition, and where the agent chooses actions based on their outcomes. In Chile, instead, the middle and upper-middle (deciles 5 to 9) seem to make choices rather independently from their outcome... Perhaps identity, subjectivity and intuition (let's call it ideology for short) play a greater role in life than Buchanan realised. In fact, the income-share of this half of the population has never increased so much as during President Allende's short period of office (from 1 to 2 in the figure), even though the majority of its opponents (and certainly the most vociferous) came from this group; in turn, its income-share has never lost so much ground as during the Pinochet dictatorship (from 2 to 3), despite this group being made of some of his most ardent supporters.

³⁵ In the CASEN survey, the cycles after '3' are far less sharp.

In turn, Figure 6 indicates changes in the income-share of the bottom 40%.

FIGURE 6

Chile: share of income of the bottom 40%, 1957-2014



- Periods and averages as Figure 5. 3-year moving averages.
- Source: as in Figure 4.

As with the income share of the middle and upper-middle strata, that of the bottom 40% did recover after the return to democracy; however, and as opposed to the downwards ratchet of D5-D9 shown in Figure 5, during the period covered by the oligarchy's 'strategy 2' this share did return to its pre-1973 levels —thanks to successful distributional policies targeted at the bottom of the income scale. In fact, it was even in an ascendant trend when the centre-left lost its fourth attempt at re-election in 2010.

All in all, 'strategy 2' was a great success for the élite; it may well have lost some of its Pinochet-share in national income, but these elements of 'strategy 2' were like a sacrifice in a game of chess, where deliberately losing one piece might help to win the game. However, as the oligarchy obviously had no intention of wearing its progressive mask indefinitely, as soon as it had succeeded in recovering a minimum of democratic legitimacy (i.e., when it finally obtained its certificate as 'born-again' democrats), it was ready to move *credibly* to a new (more distributionally aggressive) strategy —'strategy 3'.

Therefore, and despite being a political minority (but greatly helped by the ability to leverage the tailor-made political and economic scenario built by Pinochet's Constitution and his "handcuff laws"), it began its switch into a more

aggressive strategy by doing things such as defeating further labour and tax reforms in parliament (with the help of Pinochet's 'appointed' senators).³⁶

What is remarkable is that the oligarchy and its military allies managed to regain the upper hand to such an extent that it once again began resembling their preferred 'winner-take-all' scenario —**but now in a democracy**. But how were they able to do so? How did they succeed in helping create a 'spontaneous-type hegemonic consensus' around their 'unfettered-markets-supremacy-cum-trickledown' discourse? And why was the 'new' left by then not just ideologically neutralised, but also seduced into cheerleading this transformation? (If you can't beat them, join them, perhaps?)

5.- From '2' to '3': the switch back towards something resembling a 'Nash equilibrium' around the élite's extremely unequal set of distributive strategic choices, and corresponding unilateral payoffs

The first key aim of 'strategy 3' consisted of trying to stabilise the distributional outcome of 'strategy 2' —for the oligarchy *enough was enough*, as far as concessions were concerned! The second was to entrench their ideology as hegemonic. When both objectives were achieved, which coincided with the early stages of the second presidency of the centre-left, the oligarchy could finally abandon all pretence and return to distorting resource allocation and inequality in its favour (see Figure 1).

The oligarchy's remarkable success during this period tends to confirm my hypothesis that neo-liberalism may well have become one of the most effective technologies of power ever. In Latin America, the neo-liberal ideology —with its extremely successful process of 're-legitimisation' of capital— became just shorthand for "the art of getting away with extremely unequal distributional outcomes within democracies". Or, in the language of game theory, it became a technology of power capable of transforming a particularly asymmetric set of distributive strategic choices, and the corresponding unilateral payoffs, into a Nash equilibrium by convincing the majority —and in a democracy (albeit a low-intensity one)— that it was futile trying to challenge this while the all-too-powerful top income players keep their strategy unchanged.

And there was no point in challenging it not just because the chances of doing this successfully were minimal (given the artificial nature of the setting in which the game was being played —one that had been tailor-made to help the oligarchy getting the upper hand), but also because a substantial majority became **ideologically convinced** that their meagre payoff was just their fate in life! And that this type of neo-liberalism, in any case, under the current international and domestic scenarios, was the only workable game in town.

As a result, the distributional game (slowly but surely) ceased to be one of "chicken", and became one in which it was possible to achieve this most unlikely Nash equilibrium around 'strategy 3' mostly **by ideological conviction** —this is what is most remarkable about neo-liberalism as a technology of power as it could do this by means other than the old-fashioned forms of social conflict

³⁶ And this in a country where fiscal revenues were still just about 20% of GDP (OECD, 2020a and 2020b); and a country in which the higher the income decile, the lower the proportion of income paid in taxes (see Engel et al., 1999; and López and Miller, 2008). Also, as in the rest of Latin America, income tax evasion was rampant —ECLAC calculated that in 2016, tax evasion represented 7% of the regional GDP (<https://www.cepal.org/en/news/tax-evasion-latin-america-totals-340-billion-dollars-and-represents-67-regional-gdp>).

resolution. In other words, it was finally capable of achieving in democracy what it had previously only managed to do in a dictatorship.

This is a real achievement, as in most parts of the world oligarchies could only achieve this (i.e., something resembling 'strategy 3'), if neo-liberals and business leaders allied themselves with ancillary causes —culture wars, racism, misogyny, nativism, xenophobia, nationalism, and any possible right-wing populist cause. Their support for Trump and Bolsonaro are paradigmatic. However, this was not really necessary in Chile (or not anywhere near as much), where the key for its élite's success was its capacity to implement more traditional neo-liberal technologies of power, such as its ability to debilitate the rest of society by imposing an increasingly insecure life on workers and the State. These actions represented the stick, while the carrot was the promise that the payoff for the majority would eventually improve thanks to trickle-down effects, and that they should be reasonable because there was no better alternative —theirs was the only game in town.

So Chile could move from a banana-republic scenario in which the oligarchy needed a minor and corrupt Mussolini to achieve its aims, to a more sophisticated one in which military regimes —the traditional hedge against a progressive distributional challenge by the majority —could become obsolete.

Furthermore, it could do so without having to fall into the other types of bait-and-switch settings, like those mentioned above. In short, neo-liberalism at its best!

The fast economic growth during the initial phase of this period (see Figure 8 below) supports Díaz-Alejandro's (1983) critical proposition —perhaps the greatest insight of any Latin American economist ever: in terms of policy success, what matters is not so much the nature of the actual policies implemented, but **the degree of support** that they manage to gather behind a given set of policies.

However, the real challenge for the capitalist élite was that in order to sustain 'strategy 3' —and maintain that degree of support— it had to deliver high levels of economic growth and trickle-down. This was the only way to resist the natural tendency of a democracy towards a mixed and unstable distributional game that is constantly under challenge. That is, in order to manufacture consent (in Chomsky's sense), this élite also needed to show that its economic model could really deliver progress and wellbeing.³⁷

However, and inevitably, reality caught up with this 'cosy' 'strategy 3' —cosy for the élite, that is—, as in a capitalist economy **with such few compulsions**, growth was bound to decelerate, and with it most of the trickle-down.³⁸ Unsurprisingly, with the shift in distribution from profits to rents (typical of this type of 'cosy' capitalism) investment fell from close to 30% of GDP in the early 1990s to just over 20% in the late 2010s;³⁹ meanwhile, productivity growth collapsed from 3.9% p.a. between 1986 and 1998 to just 0.4% the decade before the explosion of discontent at end of 2019 (see Figure 8 below).

There is little doubt that in terms of the trickle-down effect and the well-being of the majority, 'strategy 3' failed miserably: in a country that had achieved a per capita GDP of US\$ 15,000 (US\$ 25,000 at purchasing power parity)⁴⁰, such a degree of inequality meant that in the final stages of 'strategy 3' the median net wage of Chilean workers was not high enough even to bring a family of four above the poverty line —with nearly two-thirds of female workers in this position,

³⁷ Herman and Chomsky (1988).

³⁸ On why markets need to generate 'compulsions', such as proper competition, for its dynamic, see especially Wood (2002), and Khan (2005).

³⁹ World Bank (2020).

⁴⁰ Ibid.

because, as expected in such a scenario, this median hides a huge gender gap (on average, women earned 28% less than men).⁴¹

And all this happened in a country that likes to think of itself *ad portas* of becoming a 'developed' one —a good example of wishful thinking becoming delusional.

Bearing this in mind, the most surprising aspect of this most unlikely of Nash equilibria achieved in 'strategy 3' is that while it was taking place, there was an obvious 'collective action' challenge for the majority: it could improved its payoff if only it could somehow agreed on a strategy different from the current one. But the centre-left political parties, while still commanding the support of about half of the population, did not face up even to this challenge. All they did was keep singing the praises of the mode of accumulation ingrained in 'strategy 3', while taking a bit more seriously the task of helping those who had become 'surplus to requirements' in 'strategy 3'.⁴²

The idea that 'there is no alternative' was really embedded in the spontaneous consensus around 'strategy 3'; in fact, it synthesised the fundamental core belief of the "Anglo-Iberian"-style neo-liberal discourse. And this 'taboo' had an amazing paralysing effect on the 'new' left and on the majority of the population.

In Freudian parlance, the 'totem' built around the power of 'unfettered markets', giving them an almost spiritual significance —as a symbol that is erected as the emblem of the neo-liberal tribe, one that has been converted to a kind of animistic pagan religion—, coupled with the taboo against even daring to think of alternatives (it is the end of history, after all...) is one of the most brilliant of ideological tricks ever.

Surely Gramsci must have felt revindicated. In a democracy, distributive struggles are basically won or lost at the level of ideology. Fundamentals? What fundamentals?

Also, as Albert Einstein emphasised (and Althusser, 1975, later theorised)⁴³, even in natural sciences "Whether you can observe a thing or not depends on the theory which you use. It is the theory which decides what can be observed."⁴⁴ And in the social sciences, this theory will also suggest the range of options for the econometric specification. And the circle can easily be closed as in traditional econometric testing there is the problem of "too big to fail" —i.e., in very large samples *p*-values go quickly to zero; this can mislead researchers to claim support for results of no practical significance.⁴⁵

⁴¹ Durán and Kremerman (2020).

⁴² It's really difficult to understand why élites in high middle-income countries are so reluctant to eradicate poverty, as this would be so remarkably cheap. ECLAC (2010) calculates that in six Latin American countries (including Chile), the cost of a 'one poverty line' monetary transfer to all the unemployed, all people over 64, and all children under 15 of vulnerable households would be equivalent to between 1.8 and 2.7 per cent of GDP — not such an insurmountable task! Even Brazil's successful 'Bolsa Familia' programme costs just half a percentage point of GDP (Holmes et al., 2011).

⁴³ On Althusser see also Laclau (2012).

⁴⁴ Quoted in Heisenberg (1971, p. 63). This author adds "... as Einstein has emphasized, ... deduction in [a scientist's] method runs not from facts to the assumptions of the theory but from the assumed theory to the facts and the ... data. Consequently, theories have to be proposed speculatively and pursued deductively with respect to their many consequences so that they can be put to ... tests. In short, any theory ... makes more ... philosophical assumptions than the facts alone give or imply (Heisenberg, 1958).

⁴⁵ In other words, unless the true effect of size is exactly zero, all that is needed 'to reject' the null hypothesis (even when the null hypothesis of no effect is true), and declare that there is a statistically significant effect, is a large enough sample —particularly when working with traditionally unambitious levels of significance.

6.- From '3' to '4'

The strength and weakness of the neo-liberal discourse resemble Callicles' dialogue (he is a character in Plato's *Gorgias*):

It is natural and just for the strong to dominate the weak, and ... it is unfair for the weak to resist such oppression by establishing laws to limit the power of the strong.⁴⁶

In Callicles' opinion —as in the neo-liberal critique of the post-war social democratic welfare state—, the problem (and what had to be reversed) had been that

The stronger, more aggressive and domineering by nature, had been defanged and domesticated by the new legal institutions of the weak *demos*.⁴⁷

And this is Callicles again, here trying to talk Socrates out of philosophising:

[...] for philosophy, Socrates, if pursued in moderation and at the proper age, is an elegant accomplishment, but too much philosophy is the ruin of human life. [...] Take my advice, abandon argument. Learn the philosophy of business, and acquire the reputation of wisdom. [...] Cease, then, emulating these paltry splitters of words, and emulate only the man of substance and honour, who is well to do".⁴⁸

In sum, as the capitalist élite liked to preach to the 'new' left during 'strategy 2', 'quit philosophising', 'abandon argument', get real, do an MBA! It would also help if one could convince the rest of society that the 'dissident' camp was solely made up of pedantic doctrinaires.

The debilitating component of this discourse is that 'quitting philosophising' and 'abandoning argument' really meant quitting **critical thinking**.⁴⁹ The problem with critical thinking, of course, is that it is a distancing, even debilitating, activity. It distances us from conventions, from established assumptions and from settled beliefs. It takes what we know from familiar, unquestioned settings and makes it strange. And it does so not by just supplying new information, but by inviting and provoking **a new way of seeing**.

The risk is that once the familiar becomes strange, it is never quite the same again. However unsettling, the change can never be undone —it can never be un-thought or un-known. And as many in the Latin American left know only too well, there are also huge risks involved, both political and personal. One way of avoiding those risks (particularly after so many disappointments, so much vulgarity and terror) is through a characteristic evasion: evasion as *scepticism*. Although, as Immanuel Kant (1787) reminds us, a period of scepticism can be a welcome resting place to reflect upon dogmatic wanderings, to remain there is simply to give up on moral reflection.

The point here, of course, is that despite delusional fantasies of 'oligarchic supremacy by some deserving moral right', the stronger are not so by 'nature' **but by environment**. This is the core issue of the Darwinian insight that a subset of members of a population may come to flourish relative to other members simply because they possess a feature, which others do not, that renders them relatively suited to some **local environment**. The question of the intrinsic worth of those who flourish most is not relevant to the story.⁵⁰

⁴⁶ See <https://www.gutenberg.org/files/1672/1672-h/1672-h.htm>

⁴⁷ Ibid.

⁴⁸ Ibid.

⁴⁹ See Palma (2014).

⁵⁰ Lawson (2003).

This is what leads to a crucial component of my explanation of what neo-liberalism is really about: it is a conscious and deliberate attempt to create a specific (and artificially constructed) economic environment that is most suited to those features that capital possesses and others do not —one in which a mobile and malleable agent could achieve an unrivalled dominance, which then creates the seductive force of absolute power that feeds this ideology with narcissism; one that has spellbound the ‘new’ left.

One reason for this dominance is that in this scenario, capital has easy access to mobile financial assets that provide an expedient ‘exit strategy’. Hence, its threats in the distributional game in that scenario are surely credible. It is like a kid telling the other players in a street football match that either he plays centre-forward or he goes home and takes the ball with him. Surely not the best scenario for building an effective team!

Another metaphor would be like having a puzzle made of (say) 100 pieces, but a few large ones have the option to decide what shape they would like to take, and then all the rest has to reshape to accommodate. Or, according to the great Argentinean cartoonist Quino, it is like a game of chess in which the oligarchy can checkmate its opponents whenever it likes, whatever its position on the board —which would make the game rather boring and predictable.

However, on the positive side, having an expedient exit strategy is precisely what helps the Latin American oligarchies to become more democratic —i.e., it is easier to take the risk if one is no longer geographically tied by ‘fixed’ investments (such as land in the past).⁵¹

Although the core of their accumulation will always be their home country (where else could they hope for the kind of returns they get there in the purely extractive side of commodities and some non-tradable and finance?), they can now conveniently operate in a geographically wide portfolio.

In Chile, for example, and according to balance of payment statistics, the assets of the ‘international investment position’ of the financial and non-financial private sector (not counting private pension funds) reached US\$383 billion in 2018 — about a third larger than that year’s GDP.⁵² And the foreign currency component of overall debt by non-financial corporations reached one third of GDP (about US\$100 billion) —as a share of GDP, the largest among all emerging economies with the exception of China.⁵³ And unlike China, with little to show for it in terms of investment, technological absorption, domestic product diversification and productivity growth! In fact, while in Chile the average investment per worker increased by about a factor of 3 between 1980 and 2018 —after having been stagnant for the first decade of its neo-liberal reforms—, in China it did so by more than 20 times (and according to some sources by nearly 30) —perhaps one can have too much of a good thing!

In fact, in Latin America (with the sole exception of Chile during the 1990s, as mentioned above), the rate of investment has struggled to reach 20% of GDP since the beginning of economic reforms —less than half China’s recent levels; meanwhile, its GDP-share of household consumption, mostly the result of the exuberance of the few and the ever-increasing levels of debt of the many, is currently twice that of China. Needless to say, both China and Latin America (and none more than Brazil) now urgently need to rebalance their growth, but in opposite directions.

With these levels of investment, productivity growth and product diversification, China quickly turned the tables on the European Union and the US. And this led wages to grow at such speed that the share of labour in national

⁵¹ On this issue, see Boix (2003); and Palma (2019a).

⁵² Chile, Banco Central (2020).

⁵³ Avdjiev et al. (2020).

income has grown by more than 14 percentage points since 2007 (to over 60%), with the minimum wage growing in parts of China up to 20% p.a. In Chile, instead, the labour share in national income has fallen during this period no matter how one calculates this share.⁵⁴

In Chile, the bottom line is that, rather than being invested at home, most of these funds were used by the capitalist élite to finance capital flight in the form of shifting productive capacities to neighbouring countries —where there were still significant niches for their perennial rent-seeking drive. So the assets emerged abroad, while the debts were kept nicely at home —and with the implicit government guarantees to which they have become accustomed. Whatever they say, the main aim of this capital flight is to widen their international portfolio as an essential component of their ‘exit strategy’; which, in turn, makes their distributional threats at home more credible. They are in a win-win situation, while everyone else...

This new ‘development’ strategy did certainly help deliver an odd political settlement during ‘strategy 3’, characterised by a combination of an insatiable capitalist élite, a captured progressive intelligentsia, passive citizens (at least until this most remarkable of social explosions in October 2019, led by new generations and the feminist movement), and a stalled social imagination, which was spellbound with the “absolute certainties” of the new hegemonic ideology.⁵⁵

One helpful component in all this was that in the Ibero-American tradition, societies are often run by huge state apparatuses of faceless bureaucrats prepared to follow passively whatever ideology is the order of the day —no matter how economically inefficient these ideologies may be. No South Korean, Taiwanese or Singaporean (Weberian-type) civil service here!

In fact, a paradigmatic example in Chile of this Ibero-American “faceless bureaucrat compliance syndrome” is the way in which the ‘TPP-11’ treaty was negotiated by the relevant bureaucrats;⁵⁶ they seem to be convinced that their professional duty is to be the compliant mandarins of the politicians on duty. Try explaining to those bureaucrats involved in the TPP-11 negotiations (who were happy to concede endless new rights to multinationals —and without any reciprocal obligation—, and to take the resolution of conflicts within the TPP-11 from Chilean courts to newly created international Mickey Mouse-type courts), that for a country like Chile freedom is the achievement of autonomy, when their civil service incomes depended on their not understanding! As Primo Levi wrote, the truly dangerous people are “...the functionaries ready to believe and to act without asking questions”.⁵⁷

In short, although in ‘strategy 3’ there could be only one distributional winner, a rapid (although decelerating) rate of economic growth, gains from multiple asset bubbles and easy access to an almost unlimited amount of credit initially helped confirm the ‘trickle-down potentials’ aspect of the story in ‘strategy 3’, and facilitated popular support for the unfettered-market-supremacy discourse. So much so that in this scenario, right-wing parties were even able to win a democratic presidential election for the first time in over half a century.

However, the élite did not have a high probability of winning indefinitely in ‘strategy 3’, any more than it had in any of the other distributional games it played in Chile during this period. As already mentioned, Benjamin stressed that all class societies are in a permanent state of emergency because rulers are

⁵⁴ <https://www.stlouisfed.org/on-the-economy/2017/november/measuring-labor-share-latin-american-countries>

⁵⁵ Palma (2014).

⁵⁶ See <https://ciperchile.cl/2018/03/09/el-tpp-11-el-gobierno-saliente-y-la-utopia-invertida/>

⁵⁷ <https://newrepublic.com/article/119959/interview-primo-levi-survival-auschwitz>.

always under threat; so, from time to time, the oligarchy has to 'update' its strategies of power (including important aspects of its own ideology) to counter those recurrent threats that endanger their domination. Thus, the military dictatorship was not sustainable in the long run (not least because not even the stomach of the oligarchy could digest such horror and vulgarities for ever); and the oligarchy's support for the post-dictatorship progressive distributional policies was, by definition, temporary.

In turn, 'strategy 3' was no different —and not just because 'you can fool some of the people all of the time, but you can't fool all of the people (that there is no alternative) all of the time'. Also, the inevitable deceleration of growth (particularly productivity growth) in a 'cosy scenario', such as 'strategy 3' —if only capitalists really understood what capitalism is all about!— and the excessive-greed-at-the-top that restricted the trickle-down played a crucial role in this. The social burst of discontent in October 2019 finally sent 'strategy 3' to its resting-place. It had achieved its goals (for the élite), but it had eventually become counterproductive, and the tsunami of discontent drowned it.

The natural limitation of a 'cosy' strategy of this type (capitalism without compulsions) is that the capitalist elite starts taking "cosiness" for granted; so, investment, product diversification, technological absorption, productivity growth and so on, become optional extras (see Figure 8 below). Their huge share of national income becomes a mere source of enjoyment (which includes the financial casino and capital flight), rather than the fuel that powers new engines of productivity growth.

Keynes (1919), for example, explains the contrast at the end of the 19th Century between the 'emerging' economies of the time, Germany and the US, vs. 'mature' Britain during the (investment-intensive) Third Technological Revolution, or third great surge of industrialization — that of the 'Age of Steel, Electricity and Heavy Engineering'⁵⁸:

The new rich of the nineteenth century ...preferred the power which investment gave them to the pleasures of immediate consumption.... Herein lay, in fact, the main justification of the capitalist system. If the rich had spent their new wealth on their own enjoyments, the world would long ago have found such a régime intolerable.

Intolerable indeed! At least this is the main message from Chile's 2019 social unrest, as there is little danger of finding these enlightened attributes in the newly rich anymore.

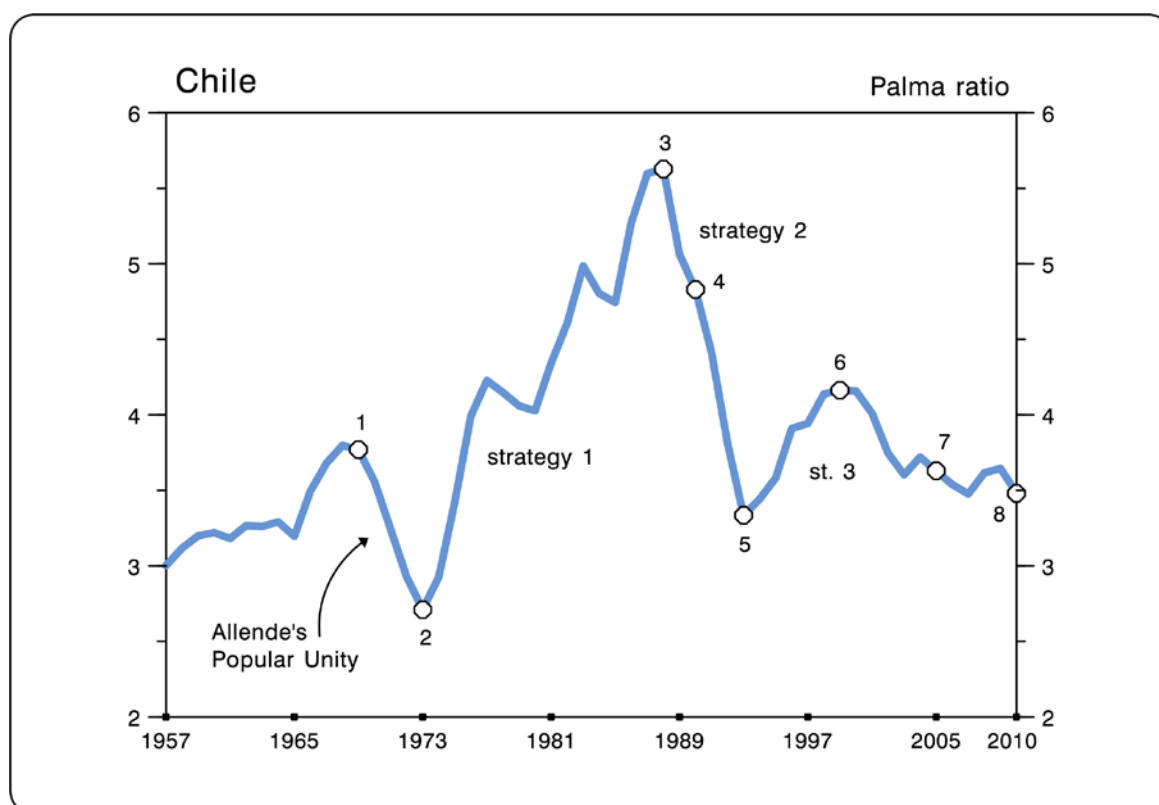
In fact, this "discreet charm" of Latin American-style bourgeoisie has now spread throughout the Western World. We are all now indeed converging, but we are doing so towards features typical of Latin-style middle-income countries, such as mobile élites creaming off the rewards of economic growth, and "magic realist" politics that lack self-respect if not originality.

Figure 7 summarises the distributional outcome of strategies 1 to 3.

⁵⁸ For a comprehensive analysis of this period, see Pérez (2002).

FIGURE 7

Chile: from 1 to 3. Changing levels of inequality as a result of the élite's changing distributional strategies, 1957-2010



• **1**=election of President Allende; **2**=Pinochet's *coup d'état* as 'strategy 1' (the inequalising-terror); **3**=Pinochet's calling (and losing) the 1988 plebiscite; **4**=first democratic government (centre-left coalition); **5, 6 and 7**=next three centre-left governments (and the emergence of 'strategy 3'). **st.**=strategy. 3-year moving averages.⁵⁹

• *Source:* as in Figure 4.

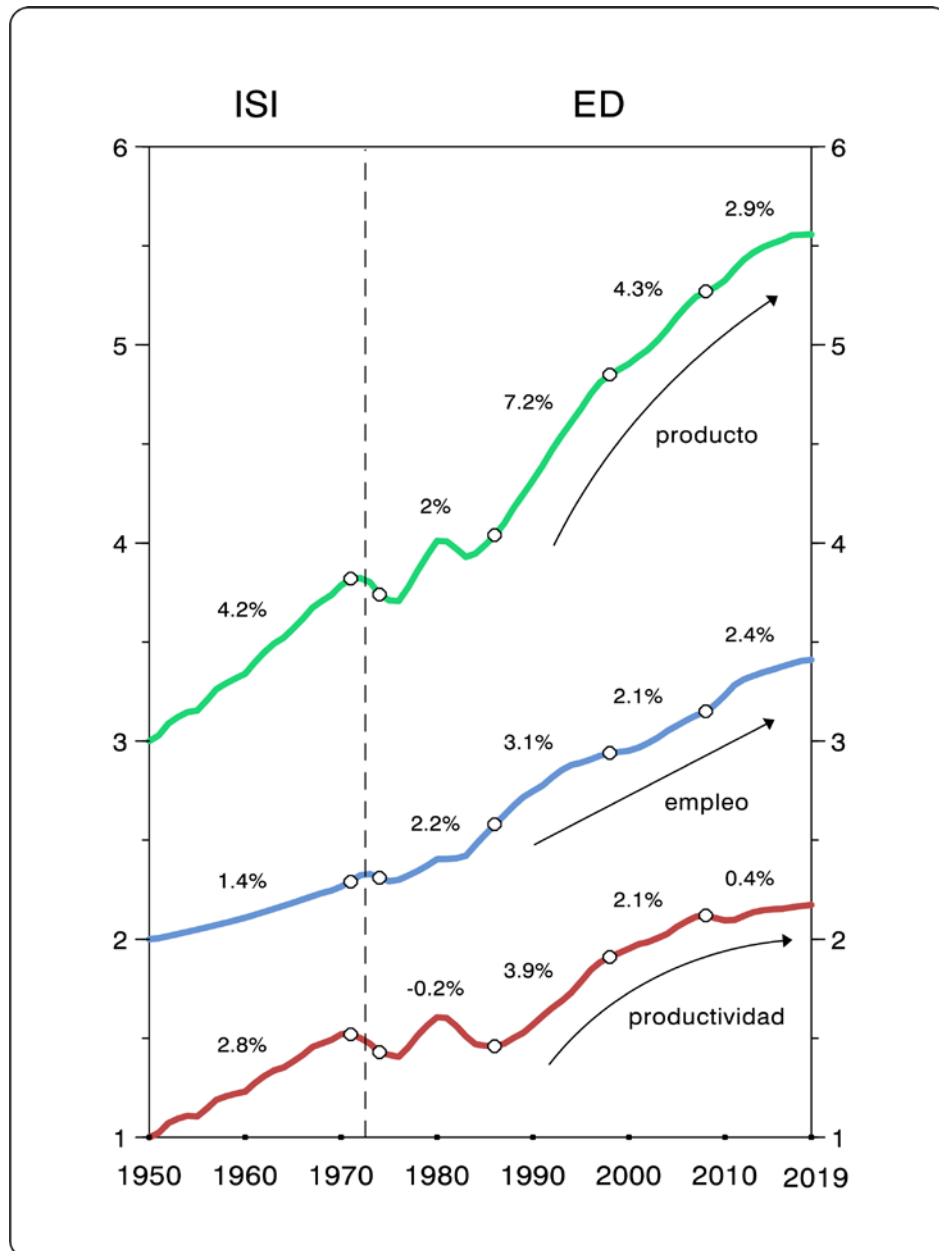
In turn, figure 8 shows the consequences of the above-mentioned Achilles heel of "cosy" capitalism: cosiness for the elite and dynamic markets does not mix well! Neither does 'cronyism' —the ever closer and mutually advantageous relationships between business leaders and 'new' left government officials, transforming 'strategy 3' into an extreme version of North's 'limited access order' capitalism.⁶⁰

⁵⁹ For a video explaining the Palma ratio as a new inequality index (published online by the Washington Post), see <http://uncounted.org/palma/>. See also <https://www.youtube.com/watch?v=wY9XFQA-McA&feature=youtu.be>. Following the logic of the Palma ratio, the World Bank (2016) coined a related statistic, the "Palma premium" —an index resembling the first derivative of the Palma ratio (as this primarily tells us about its direction of change in inequality). Also, as in econometrics the use of the Gini as dependent variable leads to misspecification and endogeneity, some new econometric work has substituted this index for the Palma ratio. The main problem of using the Gini as dependent variable is that a regression would then attempt to explain with the same set of explanatory variables two very different distributive dynamics —the homogeneity in the middle and upper-middle vs. the heterogeneity at the tails—, and this would be a specification error (Palma, 2019a). For other critique of the Gini, see Atkinson (1970); De Maio (2007); and Martín-Legendre (2018).

⁶⁰ North et al. (2007).

FIGURE 8

Chile: GDP, employment and productivity, 1950-2019



- Each series is an index number (in log-scale), with base 1 in 1950 for productivity, 2 for employment, and 3 for GDP. **DE**=“dual-extractive” model (as I call the development strategy followed by Chile since its neo-liberal economic reforms)⁶¹; **ISI**=import substituting (or state-led industrialisation); **Productivity**=output per worker. 3-year moving averages.

- Source: GGDC (2020; US\$2018, PPP).

Figure 8 confirms the idea that although neo-liberalism may well have become one of the most effective technologies of power ever, it had its Achilles heels: its preference for both an economic scenario in which there were few market ‘compulsions’, and for an emasculated State. These market failures took away key drivers of productivity growth.

⁶¹ See Palma (2019b).

If capitalism is what you want, as Keynes insisted, you must save it from this type of capitalists by implementing a progressive nationalist development agenda that seeks to inject dynamism by exercising different forms of state agencies to “discipline” the capitalist élite into investing their huge share of national income **productively**.⁶² This is the key to emerging Asia’s success! But in Chile there was no progressive nationalist development agenda in sight! Just a mild and short-lived attempt at the beginning of the second presidential term of Michelle Bachelet, nicknamed “la retroexcavadora” (the ‘backhoe’), which proved almost as short-lived as a mayfly...

As this figure shows, the deceleration of GDP growth during ‘strategy 3’ was almost entirely due to the collapse of productivity growth (from an average of 3.9% per annum to just 0.4%); that is, to the point that employment creation (mostly in traditional service sectors and construction, which accounted for 80% of the labour force, and with their traditionally low potentials for long-term productivity growth) became ‘cosy’ capitalism’s only driver of GDP growth.

The political and economic impact of this was overwhelming, proving Krugman (1994) right: although “productivity isn’t everything, in the long run it is almost everything”. So much so that when the country inevitably ran out of cheap labour (traditional services and construction had demanded cheap labour at a rate between two to three times higher than Chile’s low rate of population growth), the capitalist élite faced a historic crossroad, which was exactly the same as the one that every current developed country had faced at a similar level of development: it could confront the lack of cheap labour by updating its development strategy —in the case of Chile, by updating its dual-extractive model by searching for new engines of productivity growth, such as the industrialisation of commodities or a green new deal. Or it could just search for ‘more of the same’ by lobbying for ‘a refill’ of Chile’s unskilled labour mark —i.e., a new policy of mass immigration of cheap labour from neighbouring countries. No prizes for guessing what happen next...

The point here is that the mass influx of immigrants that followed (so far equivalent to about 10% of the labour force) was generated by a Chilean “pull”, not by an external “push” —i.e., it started with deliberate changes in immigration policy, not with political disturbances in neighbouring countries. And most immigrants came legally, by plane into Santiago’s main airport (often on specially chartered flights), in a way that ended up being a paradise for human trafficking gangs, who organised the logistics, the transport, the paperwork, and then profited from the horrific conditions in which many of these immigrants ended up living in Chile. All immigrants needed to get a tourist visa when arriving in Chile was the return plane ticket, an identity document, and a little bit of cash (to prove that they were “tourists”) —all of which were often provided by the trafficking gangs. Then, a labour contract would suffice to obtain a work permit and a temporary resident permit —again, a contract that was often provided by the same gangs.

Moreover, no one pushing for the new immigration policy seemed to have worried about the complete lack of spare capacity in housing, health service, public education, transport, and all those basic services that would be desperately needed by these immigrants.⁶³ Cheap labour has to be cheap! So, with the cheap-labour-intensive model with (practically) no productivity-growth being given a new lease of life, ‘more of the same’ growth via just employment creation was on the cards. As Voltaire had emphasised (see epigraph), the comfort of the rich (including in the production sphere) depends upon an abundant supply of the poor.

⁶² On how Korea did this during its process of industrialisation, see Chang (1993).

⁶³ Palma (2019b).

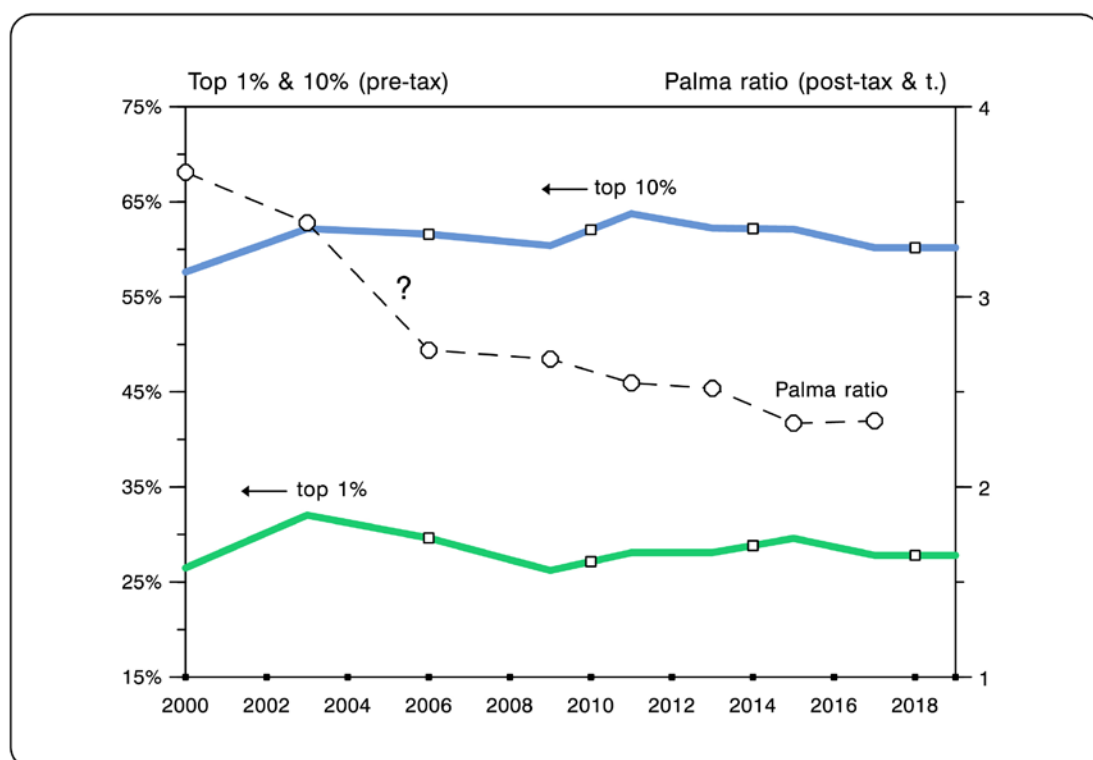
However, it was precisely this ‘more of the same’ that meant the neo-liberal model was totally unable to update itself when its existing engines of growth (mere extraction of commodities and cheap services) had run their course. “Cosy” cum ‘crony’ capitalism —an its limited access order—, had become self-destructive. The oligarchy has no one but itself to blame for ‘strategy 3’ having become counterproductive for their own interests.

This lethargy of insisting on doing just ‘more of the same’ regardless reminds us of Conrad novels where, as in so many sea stories, the main enemy of creativity is stasis. It is, in fact, the deadliest thing of all.⁶⁴

Finally, and as opposed to what household surveys indicate, new pre-tax data indicate that ‘strategy 3’ was far more distributionally successful for top earners than it had been reported so far —casting further doubts on Chile’s supposed declining inequality. (Figure 9).

FIGURE 9

Chile: shares of pre-tax income of the top 1% and top 10%, and the Palma ratio of post-tax and transfers income, 2000-2019



• **t.**=transfers. Circles indicate years when the Casen household survey was carried out; squares indicate presidential periods.

• Source: WID (2020), based on De Rosa et al. (2020), for top 1% and 10%; and Palma (2019a) for Palma ratios.

As the figure suggests, ‘strategy 3’ did help the top 1% and 10% keep their income-share stable at a level still similar to where Pinochet left them; which now are even higher than Brazil’s (see Figure 3 above). Furthermore, it is difficult to believe that in a country with such a low and regressive system of taxation, the widely reported drop of the shares of post-tax income at the top is anything but

⁶⁴ Segal (1997).

the growing inability of household surveys to capture the income of the rich in this growingly financialised —and fiscal paradised world.

And if the share of the top remained basically stable, a drop in the Palma ratio of the speed shown in Figure 9 (especially towards the latter period of Ricardo Lagos' presidency; see question mark in the figure) would have required an increase of the share of the bottom 40% of about twice the level reported in these surveys.

Therefore (as in the case of Brazil in Figure 3 above), there is plenty of room for scepticism regarding the much publicised supposed decline in Chile's inequality.

In sum, 'strategy 3' may well have become an abject failure in productivity matters (ending practically in a 'Ricardian-type' stagnation; see Figure 8); it was nevertheless remarkably successful in distributional matters for the rich —until an outburst of popular discontent put a sudden end to it with a display of social power not seen in Chile since the one that defeated Pinochet in his 1988 plebiscite. The power of the young (enraged by the hopeless future on offer under this strategy), and the feminist moment (which had had enough of gender abuse at every level)⁶⁵, broke the neo-liberal ideological spell: the ('there is no alternative') emperor had no clothes.

7.- 'Strategy 4': from the ideological narcissism of 'strategy 3' to the élite's sudden need to idealise the European 'new' social democracy

Although this new distributional switch clearly involves many issues, there can be little doubt that the key one is economic reality catching up with the lack of productive dynamism of ('cosy' and 'crony') 'strategy 3'. Also, new technologies of social communication have helped improve social cohesion among the majority. Previously, the elite's greater capacity for collective action gave it the upper hand in games of chicken; but new technologies of communications, as the social unrest in Chile demonstrates, became a game changer for the majority!

The explosion of social unrest in October 2019 was quickly followed by the emergence of the pandemic, which provided a distraction from the social discontent. However, as poverty and unemployment grew rapidly, while the centre-right business-friendly government struggled to respond, this distraction did not last. In turn, insult was added to injury as almost all the great fortunes continued to expand as in the best of time, helped by the "perpetual mania" of the financial casino (Palma, 2020b). When the plebiscite to change Pinochet's Constitution took place in October 2020, it gained 80% support.

From the perspective of this work, one of the key impacts of the pandemic was to throw all kinds of inequalities into stark relief. For example, while in a middle-class neighbourhood (Ñuñoa) the two main reasons for requesting a circulation permit during the quarantine were for people to go to a supermarket and to walk their (pedigree) dogs, in a popular neighbourhood (La Pintana) these were for attending funerals and visiting relatives in penal facilities. In addition, the low levels of internet coverage in the latter, just 13%, forced people to leave their homes even if they could otherwise have worked or studied from home.

The combination of the explosion of discontent and the pandemic led to great anxiety among the élite —and in many to an outright panic— that Chile would return to being politically unmanageable as soon as there was some resemblance of normality. For a respected right-wing analyst, for example,

⁶⁵ Its slogan, "El estado opresor es un macho violador" (The oppressive state is a rapist macho) said it all (<https://www.youtube.com/watch?v=tB1cWh27rml>).

The greatest fear [...] is not the coronavirus, which will claim many lives, but it will pass [...]. Nor is it the imminent economic debacle, which will also finally recover [...]. [The] greatest fear [...] is an unmanageable social group that has abandoned the basic rules of communal life [...].⁶⁶

Faced with these uncertainties, some politicians and business leaders began to idealise the European 'new' Social Democracy as a way out of their strategic impasse, hoping it might help reactivate economic activity while ensuring a minimum of protection and social peace ('strategy 4').

For example, the presidents of both main business associations (The Confederation of Production and Commerce, and The Society for Manufacturing Development), contradicting everything that both business association had preached for generations (especially since the neo-liberal reforms), began to call for a European-style new social democratic model.⁶⁷ Even some intellectuals from that political orientation began to publish their "Social Democratic Manifestos", to prevent "[...] future governments from going from [social] explosion to [social] explosion".⁶⁸ The finance minister of Chile's current right-wing government expressed a similar opinion, and the main right-wing candidate for the next presidential election (a Chicago Boy and one-time Pinochet favourite) also, for the first time, defined himself as 'social democrat' —and even in favour "of a new and stronger state [capable of] guaranteeing social rights".⁶⁹

Not surprisingly, some on the 'new' left became really upset with this apparent infringement on their intellectual property rights!

However, it is precisely the highly inefficient and probably unsustainable inconsistencies between the economic and social agendas of the European 'new' social democracy that made it so attractive for the élite (see Appendix 2). In this new scenario, while a new social democratic economic agenda could still aim at delivering more of the same, a new social agenda could give a new lease of life to their now fragile neo-liberal model. Furthermore, they have an ace up their sleeve: in this financialised world, instead of having to pay for the extra social protection with new taxes, additional public sector borrowing can always save the day. Therefore, for the Latin American business community, a switch to 'strategy 4' could be another win-win situation: it could help re-legitimise its neo-liberal rentier model by making it a bit more civilised, and public bonds (instead of taxes) could finance the much-needed social peace and a minimum degree of equity. How had this not occurred to them before?

Basically, this would be a way to square the circle: powerful agents could continue to manipulate the product and financial markets at their pleasure (which includes continuing to extend the 'market' into hitherto unacceptable, even inconceivable, spheres of social life —those that have already generated some of the most inefficient activities in the economy), and higher deficit spending could facilitate the "herd immunity" necessary for social peace.

From this perspective, the new strategy makes complete sense, and the dwindling number of people within their group that still rejects it are driven by the self-destructive power of fundamentalism. The most attractive element for the more enlightened right wing is that this new alternative, together with offering a minimum of social peace and some equality, allows them to maintain

⁶⁶ <https://www.latercera.com/opinion/noticia/el-miedo/SS57SUH65JGWXEE4VDXJD5N2W4/>

⁶⁷ See, for example, <https://interferencia.cl/articulos/entrevista-juan-sutil-desde-el-punto-de-vista-social-probablemente-chile-tiene-que-avanzar>; and <https://kiosco.latercera.com/reader/03-08-2020-la-tercera?location=31>

⁶⁸ <https://www.elmostrador.cl/destacado/2020/07/24/un-manifiesto-social-democrat/>

⁶⁹ <https://www.emol.com/news/National/2020/08/24/995890/be-social-democrat-definition-Lavin.html>

the Buchanian aspects of their model, of which Pinochet's Constitution and its "handcuff laws" are a paradigmatic example.

For Buchanan (1993), it is big business who really needs "social protection", and their property rights can only be guaranteed by imposing constitutional guarantees. Buchanan viewed society in a rather paranoid way, as in eternal conflict between "creators" (entrepreneurs) and "looters" (everyone else) who would have the former constantly besieged. In his work he repeatedly warns of the danger of "parasites" and "predators" on the lookout for "innovators." Therefore, it is the owners of big capital who actually need 'social protection', and their property rights could only be guaranteed by (Chilean-style) **constitutional limits** to change.

Also, implicit in Buchanan is the idea that as part of their 'social protection' big business should have the privilege of being somehow above the law. This idea has some resemblance to Carl Schmitt and Giorgio Agamben's "state of exception", except that it is not related to the sovereign's ability to transcend the rule of law, but that of a group in society. Also, this 'exceptionalism' is not intended to be temporary: in the name of Buchanan-style understanding of 'the public good', it is intended to be a permanent state of affairs.

One Chilean example of this 'exceptionalism': why fear prosecution, when—if convicted for (say) fraud— instead of going to prison one may be just sent back to university! A judge recently sent corporate executives convicted of a major tax fraud on a one-semester course in corporate ethics (with the condition that they had to get a passing grade!). The same happens in developed countries; in this 'too-big-to-jail' world, when HSBC became the bank of choice of Mexican drug cartels, or Standard Chartered of those on the official terrorist list, they just got a fine and no one went to prison. In turn, when Purdue Pharma and other drug-makers encouraged over-prescription of opioids, leading to overdoses and addiction that according to US government data resulted in 450,000 overdose deaths from 1999 to 2018 (half again as many people than all fatalities so far in the current pandemic), there was just a fine and no one went to prison—even if they agreed that they "knowingly and intentionally conspired and agreed with others to aid and abet" doctors dispensing medication "without a legitimate medical purpose".⁷⁰ Furthermore, the court had no problem with the Sackler family having transferred (often through questionable means) more than US\$10bn out of the company between 2008 and 2017.⁷¹

As a law professor states (commenting on how the Trump Administration spared corporate wrongdoers billions in penalties), "There's no reason anymore to fear prosecution for committing serious corporate crimes".⁷² In fact, in a Buchanan-style thinking this would not be just the mere exercise of state capture by big business, but something that has a perfect logic in the sense of untying the hands of "creators" and "innovators".

In Chile, as in the rest of Latin America, this influence of Buchanan also impregnated the ideology of the 'new' left; since the transition to democracy, they have spared no effort in apologising for their supposed "predatory" past (such as having been in favour of agrarian reforms, nationalisation of natural resources, and so on).

This growing asymmetry between the economic and social agendas also took place within the Chilean Christian democrats; in the 1960s, its first President,

⁷⁰ <https://www.ft.com/content/8112c484-c8f9-49f8-8d6d-bffe99ccb59>; see also <https://www.ft.com/stream/e0c6c996-1c60-4ac0-8e96-ecb154217b20>

⁷¹ See <https://www.bbc.co.uk/news/business-54636002>; and <https://uk.reuters.com/article/us-usa-opioids-litigation/mckesson-says-states-seek-21-billion-from-drug-distributors-in-opioid-settlement-idUKKBN27J1UC>

⁷² <https://www.nytimes.com/2018/11/03/us/trump-sec-doj-corporate-penalties.html>

Eduardo Frei Montalva, had an economic agenda which was closely articulated with its social one: agrarian reforms and the partial nationalisation of large copper mines went hand in hand with policies for social protection and social empowerment (the “Promoción Popular”, or “Popular Empowerment” policy). However, in the 1990s, during the presidency of his son Eduardo Frei Ruiz-Tagle, while the social agenda remained similar to that of Frei senior (although implemented with many more consultants), the economic agenda tried to build a future which was the exact opposite to that of his Father’s agenda. And since these agendas pointed in opposite directions, they obstructed each other.

And the support of most of the centre-left for these constitutional barriers that defend the property rights of “creators” is done regardless of the rather ‘uncreative’ way in which many of these supposed “innovators” acquired their assets —such as in ‘piñatas’ of public corporations and of natural resources during the highly corrupt neo-liberal reforms, piñatas in which access was restricted to courtiers of the regime (others need not apply).⁷³

The open question, of course, is whether in Latin America this ‘strategy 4’ would be as effective a mechanism for making a rentier neo-liberal economic agenda more acceptable as in Western Europe. Political settlements of this kind are surely bound to be more fragile in the periphery than in the centre. Also, perhaps ‘strategy 4’ came a bit too late in Latin America, just as the aristocratic concessions did in late 18th-century France. Latin American oligarchies will surely need now some truly fancy footwork (and the appropriate ‘collective action’) to make this new strategy work!

Conclusions

This paper tries to answer the question why is it that the rich stay rich no matter what? Is Latin America’s huge inequality (and in particular Chile’s) a reflection of a specificity of ‘fundamentals’ or particular interactions between power structure and choice? Is its high market and disposable income inequalities the product of somehow ‘exogenous’ factors (as in most neo-classical analysis) or of complex interactions between political settlements and market failures? How do we get through the veils obscuring these interactions and distorting our vision of the **self-constructed** nature of its artificially-high levels inequality? Has neo-liberal globalisation-cum-financialisation broadened the scope for “distributional failure”?

As discussed above, one key answer to those questions is that rather than thinking (as in most neo-classical narratives) about the possible **concrete effects** that well-known factors may have on inequality (e.g., technology, social mobility, education, and so on), it would be more illuminating to try to understand the **concrete expressions** that these factors may find in actual experiences of inequality, such as Chile’s.⁷⁴ In fact, some of the pieces of the distributional puzzle may well be the same in different countries, but the way they fit together may well differ —sometimes significantly.

As initially discussed in my first paper, written while I was still a graduate student (Palma, 1978), and developed further in Palma (2016b), the analytical challenge in subjects such as inequality is not about building “mechanico-formal” theories, from where ‘general implications’ can be abstracted. It is about developing methodologies for the analysis of concrete situations of phenomena

⁷³ See, for example, Mönckeberg (2015); Gárate (2012); and <https://www.ciperchile.cl/2013/09/12/%c2%bfhow-long-to-wait-for-the-Chicago-boys-associates-to-answer-for-the-loot-that-some-took-away/>

⁷⁴ For a more detailed critique of neoclassical distributional models, and of their econometrics see Palma (2019a). For other critique of the Gini, see Atkinson (1970); De Maio (2007); and Martín-Legendre (2018).

such as inequality —in this case, for the analysis of Chile's *concrete experience* of inequality.

The question which we should ask ourselves is why, it being obvious that the capitalist economy tends towards a greater level of inequality (and this mainly because the élite has the option to construct **several routes** to get the upper hand in the distributional struggle —rather than because of neo-classical issues such as “ $r > g$ ”); why, it being obvious that we have embarked on a process of growing internationalisation and financialisation; that societies are divided in groups with antagonistic interests, and that the particular is to a certain extent conditioned by the general, why with these premises we have not gone beyond the partial —and therefore *abstract*— characterisation of inequality.

A key lesson from the Chilean experience is the key role played by **choice** in inequality; for example, although Chile has the same GDP per capita and average wage as in Croatia (World Bank, 2020), it has a median wage that is only half Croatia's (Duran and Kremerman, 2020). Surely this is not so because some exogenous ‘fundamentals’ have forced Chile to have a much higher degree of wage inequality —i.e., surely this is not the mechanical consequence of Chile's abundance of natural resources, its levels of education, its particular problems with skilled biased technological change, and so on, but basically because of choice. Choice in the sense that in terms of inequality there is no room for claims that we are just innocent bystanders at the mercy of ‘exogenous’ distributional forces. This choice, of course, is not absolute but it is normally (although not always) taken within the parameters of the interaction between our history, politics and institutions with some of those fundamentals. As already suggested, for an agency to succeed it needs to understand structure!

For example, Chile spends twice as much as Croatia in education in terms of its percentage of public expenditure and its tertiary enrolment is one-third higher; spends nearly half as much in health in this indicator; has a much higher rating in Moody (A1 vs. Ba1), S&P (A+ vs. BBB-) and Fitch (A- vs. BBB-); has a much lower level of corruption; its State is less ‘fragile’, and so on, but its Palma ratio is 2,8 (and Gini 48), while in Croatia the Palma ratio is just 1.1 (and Gini 31).⁷⁵ Perhaps the fact that its rate of homicides (although very low for Latin American standards) is four times higher than Croatia's is a much more telling indicator as far as Chile's actual choice of inequality —and of the way in which we articulate conflicts in general— than what rating agencies can tell us about both countries.

Surely no ‘external’ force has compelled Chile (which such high middle-income level) to have a median net wage not high enough even to bring a family of four above the poverty line, with nearly two-thirds of female workers in this position —should we also blame gender discrimination on some ‘fundamental’, or external force?

In other words, nothing reveals more transparently who we truly are in Chile as a society than the inequality we collectively choose to construct. The bottom line is that in Chile we deserve the inequality we have. And this it's as self-defining an act as it can be!

Another lesson from the Chilean experience is that in countries with such artificially created high level of inequality, most routes available to the élite to get the upper hand in the distributional struggle are associated with different degrees of economic inefficiency.⁷⁶ Mostly (but certainly not entirely) because of this, these routes or élite-strategies sooner or later become losing games *if played indefinitely*.

⁷⁵ World Bank (2020); and Palma (2019a).

⁷⁶ See Figure 22 in Palma (2019a).

Therefore, the secret of success for the élite has been its flexibility and internally cohesion when playing their sequence of 'losing strategies' that wins —i.e., the Parrondo paradox. Perhaps Chile's greatest contribution to the analysis of inequality is that these phenomena have taken place in a fairly transparent form.

In turn, as discussed above, from the perspective of the interaction between artificially-created inequality and economic inefficiency what's happening in the high-income OECD indicates that they now seem almost infatuated with their process of "reverse catching-up" with unequal middle-income countries. That is, they now seem determined to mimic the Latin American distributional process by which (in a Ricardian-style) there is an artificially created shift in distribution from profits to rents, leading to a slowdown in productivity growth. Furthermore, given this squeeze in operating profits, capitalists are increasingly seeking to generate as much as their income via (also often artificially-created) rents as possible.⁷⁷

So, life is no longer that easy in the OECD now, with a family and a rentier oligarchy to support —should I say 'Welcome to the Third World'?

If the above is the case, the relationship between inequality and underperformance would be an indirect one as both phenomena would be the outcome of a third factor: a distributional drive favouring rents at the expense of operating profits while keeping wages at best at a standstill —even before the crisis created by the pandemic, real wages were lower than in the early 2000s in about two-thirds of households in 25 advanced economies —more than 500 million people. In the UK, for example, during this period real wages had their worst performance since the Napoleonic Wars.⁷⁸ In turn, in the US average hourly real earnings were kept stagnant since Reagan's election in 1980.⁷⁹ And while the S&P500 was soaring more than 320% between 2009 and mid-2018 —the longest bull market on record, which created more than US\$18tn of (virtual) wealth—, the median US household wealth was actually falling. @And as monetary authorities in the OECD —the "new alchemists"— now think that their main aim in life is to make sure that 'the rich stay rich', bull markets have become schizophrenically detach from investment: if the US had continued with the same share of investment-to-GDP as pre-Reagan, over US\$ 1 trillion more would be invested per year.⁸⁰ In fact, *net* private investment all but disappeared.⁸¹ As in a fitting "reverse catching-up" with Latin America, now in the high-income OECD the higher the share of income appropriated by the top, the lower the proportion of that income that is returned to the economy in a productive manner.

The analytical challenge, therefore, is to understand the mechanisms which help the rentier to get the upper hand in highly unequal middle income countries, such as Latin America —and now in the high-income OECD as well—, and the specificities of this phenomena in each historical circumstance —where, as Chile indicates, history, politics and institutions will undoubtedly play a crucial role.

The key point here is that on the subject of inequality, what matters most ***is taking responsibility for our distributional choices***. Certainly, no 'exogenous' force has forced the OECD to 'bananise' its market inequality —and

⁷⁷ For the current role of financial markets and monetary authorities in helping rentiers (in the form of shareholders and executives) getting the upper hand in non-financial corporations, see Palma (2020b).

⁷⁸ Palma (2019a), and McKinsey Global Institute (2017).

⁷⁹ Palma (2020b).

⁸⁰ Ibid.

⁸¹ US Bureau of Economic Analysis (2020).

with it, its economic performance (see Appendix 2). Surely it is their choice, and as self-defining an act as it can be!

As for Latin America's "Southern-style" distributional scenario, it has so far proved to be something resembling a stationary process: no matter what the rest of society has thrown at the oligarchy, their 'jogo de cintura' has been up to the task. Therefore, so far the impact of shocks (no matter how huge) have had a short-lived impact (one that has declined over time).

And this 'stationary process' has also spread to our imagination and culture, as Latin America is now a region whose critical social imagination has stalled, changing from a post-War prolific period to an intellectually barren one since the 1980s reforms. Of course, it could be argued that what happened in Latin America is not really that different from what has happened in the rest of the world post-1980, both developed and developing. One could even argue that the demise of critical thinking has spread around the world almost as a pandemic, transforming critical thinkers into an endangered species. The specificity of Latin America is that the downswing of this cycle of critical thinking has been particularly pronounced.

From this perspective, we have been left with both an oligarchy which is only interested in cleverly switching between distributional strategy (so as to construct a winning distributional game), and an intellectually stationary 'new' left that refuses to understand that in order to develop more sophisticated technologies of power it needs more sophisticated forms of knowledge. This is particular so in the economic sphere, where their choice of monotonously repeating 'more of the same' after the transition to democracy has proved to be counterproductive for their aspiration of becoming a hegemonic force. In short, they have been unable to build a proper *identity* via a successful "discursive articulation" between their economic beliefs and a reality inhabited by a plurality of agents and struggles.

Thus, in this "Gatopardian" stationary mode, everything has been allowed to change (e.g., the transition to democracy) so that everything *that mattered* to the élite could stay just as it was. Whether Chile's October 2019 social outburst (now mixed with the pandemic) proves 'a shock too far' for its oligarchy, or whether it will manage, yet again, to pull another rabbit out of its distributional hat —this time a social democratic rabbit— is Chile's known unknown.

The real mystery, however, is why oligarchies of this type can have such Muhammad Ali-style fancy footwork on distributional matters, while in economic matters they display the clumsy footwork of an elephant —such as still being stuck in its glaringly obsolete 1970s neo-liberal model, one resembling the early, and most primitive, Washington Consensus. If in one sphere they are the masters of "political articulation", in the other they have shown the manoeuvrability of an oil tanker.

A substantial component of the answer to that question, as discussed above, is that there are hardly any ways to reshape the structure of an economic 'system' with so little entropy: in how many ways can one redesign the structure of its economy, so that it can move 'forward in time', if one can't change the fundamentals of its *status quo* — that those at the top continue to corner an enormous share of national income, while seizing the low-hanging fruit they favour. In other words, (as in Coleridge's Ancient Mariner) the oligarchy's fancy footwork in economic matters is more problematical, as it is stuck with a (rentier) albatross hanging around its neck. In this sense, as in FDR's New Deal, what is required today 'to move forward in time' is not only a new set of Keynesian economic policies, but also a package of institutional reforms able to change the whole environment in which economic activity takes place.

Regarding their distributional strategies, perhaps the Latin American capitalist elite have now set themselves too ambitious a challenge: how to retain

a lion's share of national income while ensuring that their rentier (and ever more inefficient) economic agenda is sustainable in time, as the majority are now prepared to challenge them credibly. Perhaps through 'strategy 4' —and its idealisation of the European 'new' social democracy— they might overreach, and despite their skills and experience, their "fancy footwork" may fall flat.

Furthermore, this time the help of the 'new' left is not as useful as it was during 'strategies 2' and '3', as this group has lost most of its political clout. And as Adorno (1951) remind us, this is no minor point as domination is so much more effective when "... it can delegate the ... violence on which it rests to the dominated".

Basically (and as I analyse in Palma, 2020a), in Latin America both the elite and the majority are now trapped in what I have called a "Gramscian Moment", when the old fades, but the new fails to be born. That is, when elite loses its legitimacy (and with it, capacity to get the upper hand), and alternative discourses are unable to gather sufficient credibility. In this interregnum, as Gramsci (1930) warned us from his cell in a Mussolini's jail —and as many in Latin America are experiencing themselves, especially in Brazil—, it is almost inevitable that in the intervening time "there will appear a wide variety of harmful symptoms". For Gramsci, a strong hegemony is fundamental for states to move forward —the lack of it makes societies resemble drifting boats!⁸²

In sum, had the Latin American elite's plasticity of imagination in distributional matters been replicated in the economic sphere —as opposed to being translated into a mere compulsive rent-seeking drive—, its economy (and more) would not be trapped ever deeper in the quicksand of inertia —my definition of a "middle-income trap"—, of which Chile is a paradigmatic case.⁸³

The Freudian opposition between the creativity inbuilt in the instinct toward survival and the innate self-destructive drive of human beings seem to play out rather transparently in the spheres analysed in this paper —namely, in the recurrent conflict between the Latin American elite's remarkable "ability to persist" and its compulsive (as well as self-destructive) rent-seeking drive.

⁸² Joseph (2002).

⁸³ Palma (2019b).

Appendix 1

The Latin American 'new' Left

As suggested above, what is crucial to my narrative is that on top of the usual *de facto* political power that the capitalist élite has from asset concentration, from lobbying power, from being able to solve its own problems of 'collective action', from its skills at building political alliances with the middle, and so on, an important component of its distributional success has been its remarkable capacity to build hegemonic consensuses around its own interests. The 'new' left is just one of its casualties.

In Latin America and many other parts of the world the 'new' Left is characterized by having concluded (a little too eagerly) that, with current domestic and international constraints, it would not be possible to assemble the necessary social constituencies for progressive political agendas.

The history of the global South teaches us that this type of agenda requires a sufficiently strong domestic constituency behind it in order to be able simultaneously to take on all the 'usual suspects' (in the form of international and domestic forces) that are fiercely opposed to it. This constituency is required, for example, for the State to be able to impose East Asian-style 'discipline' on capitalists (and sometimes on workers) so as to be able to reach the low levels of inequality ***in the sphere of production*** found in countries such as Korea and Taiwan (see Figure A2.2 below).

Although in some cases —such as the paradigmatic examples of Mandela in South Africa, Lula in Brazil and Aylwin and Lagos in Chile—, centre-left coalitions in the South clearly had the opportunity to build such a large constituency, they nevertheless threw in the towel too easily. So, they gave up their progressive economic agenda and abandoned the economy as the fundamental site of the struggle —eventually conceding practically all the terms of the economic and distributional debates.

In other words, as the 'new' left believed that it could not get political power to implement its own progressive economic agenda, it then tried to gain power to implement someone else's agenda instead —but more efficiently and with a human face. It thus sought political power to implement *de facto* what Chico de Oliveira has called an "upside-down hegemony".⁸⁴ In short, neo-liberalism, as an ideology, has proved to be such an effective technology of power that it has paralysed most of its opposition. That is, borrowing from Kafka's 'The Silence of the Sirens' (1917), the (inequalising) sirens have, up to now, had a still more effective weapon than their song, namely the (ideological) silence of their 'progressive' opposition.

Ultimately, according to Sartre's concept of *mauvaise foi* (bad faith)⁸⁵, I believe that a key component of the 'urgent necessities' argument used by the 'new' left all over Latin America, but especially in Chile and Brazil (and also in South Africa, incidentally) to justify abandoning radical economic and redistribution policies for 'prudent' and 'well behaved' market-friendly ones, was as an exercise destined to deceive others as well as themselves into believing that the transformation of society had become the ultimate unacceptable risk.⁸⁶

⁸⁴ Oliveira (2006). On how the Latin American 'new-left' has lost its ideological compass, see also Palma (2014).

⁸⁵ Sartre (1993).

⁸⁶ For Sartre, 'bad faith' is the habit that people have of deceiving themselves into thinking that they do not have the freedom to make choices for fear of the potential consequences of making a choice.

Thus a key component of its 'new-look' pragmatism was never to say or do anything that might wake the socialist ghosts of the past.⁸⁷

When Mrs Thatcher was asked in one of her last interviews what her greatest political achievement had been, her answer was clear-cut: the transformation of the Labour party into the 'New Labour' of Blair and Brown. If Pinochet had had the brains to understand this, he might have said the exact same thing about the 'new' left in Chile. It's a good example of how neo-liberals succeeded in "manufacturing consent".

The most telling sign of success at this, particularly in the economic sphere, as Žižek (2008) reminds us is when "one starts telling stories of others as if they were one's own".

As I discussed somewhere else⁸⁸, the current political project of the 'new' left could even be called an "inverted utopia". If utopia is that scenario in which it is not possible to do what one imagines, the opposite (the inverted utopia) would be when one is not capable of imagining what one is actually doing.⁸⁹ And this relates to what is discussed above relating to the way in which the 'new' left did that necessary Gramscian ideological integrative effort of elements of opposing ideologies: instead of doing it in an imaginative and creative way, it did so in a lazy, often opportunistic mode, letting the new neo-liberal economic ideology simply replace its previous ('post-war-type') social democratic ideology. In other words, in an 'inverted utopia' scenario it is as if one gets detached from what one is actually doing —especially in economic matters.

Pascalian philosophy helps to understand this; what the 'new' left did was to pursue the ritual: pretend that you believe and credibility —and belief— will follow. That is, if at the beginning they did not really believe in the neo-liberal model, a rigid devotion to the liturgy would end up believing for them. The key was not to mix what was done with what was said to be done. What was needed was to detach speech from reality.⁹⁰ And then create false dichotomies: either you were a mere 'nostalgic of the past' or an 'absolute convert'. Good sense would indicate what 'should' be done —the secret was to do it with automaton regularity; thus routine would become credibility and credibility would turn into faith. In short, do 'as if' you didn't know. Undoubtedly, in this ritual there is an important element of pragmatism, but there is also the advantage that automatism helps to give up little by little previous convictions (almost) without realising it. And, as Pascal's 'materialist theology' tells us, in the end automatism always ends up taking the mind with it!

In sum, even if one were to agree with the 'new' left that there was little option in Chile during the transition to democracy but to accept a political settlement of the kind found elsewhere in Latin America and in South Africa, and even if one understands that part of this strategy's logic was both to tell 'stories' to their base and to tell 'stories' to the capitalist élite and international financial markets (in order to conceal their initial reluctant acceptance of the neo-liberal model), what is truly amazing is how easily the 'story-telling' convinced the story-tellers themselves!

⁸⁷ See Arantes (2007).

⁸⁸ <https://www.ciperchile.cl/2018/03/09/el-tp-11-el-gobierno-saliente-y-la-utopia-invertida/>

⁸⁹ See also Arantes (2007).

⁹⁰ Ibid.

Appendix 2

A2.1.- The post-war social democracy vs. the 'new' (post-Thatcher and Reagan) "Third Way"

In the post-war social democratic thinking, and even before the end of the war (as in the meeting at Breton Woods), there was one key idea at the centre of the analysis (which is exactly the same that is most relevant to Latin America's current situation): the only effective way out of that disaster was **to restructure to reactivate**. This implied the need for new economic and social agendas, which should be designed in an intimately articulated way, so that they might both be enhanced by their interaction. This symmetry between the two agendas became the hallmark of this strategy, and one of its main strengths. Conversely, asymmetry between the two became the defining trait and greatest weakness of "version 2.0" of this strategy in post-1980s neo-liberal Europe. The economic agenda would point in one direction, and the social agenda in the other.

A2.2.- The neo-liberal crosscurrents of the '70s

One way to visualize the resurgence of neo-liberalism during the 1970s is that the stagflation post-73 awakened the destructive power of fundamentalism; those who worshiped unfettered market forces had been waiting for their chance to revenge on the previous success of the Rooseveltian-Keynesian "heresy". Neo-liberals feared that that success could annihilate belief in free markets, threatening a return to a primitive analytical chaos that would destroy understanding and eliminate meaning.

This fear brought into play the destructive instincts, since the worst part of the Rooseveltian-Keynesian heresy (and of structuralism in the periphery) was its indisputable successes in restructuring and reactivating the world economy after the war, both north and south of the Equator.

For this reason, the challenge for neo-liberals was not to overcome Keynesianism creatively, but to erase every last vestige of its existence. When the main ideologue of the Brazilian reforms was asked about the main aim of these reforms, he replied: "To undo 40 years of stupidity [besteira]". Adding, "Now you are either a neo-liberal or you are a neo-idiot [neoburro]." This attitude of 'undoing stupidities' —of multiplying everything by "minus 1"— was what led these neo-liberal reforms to become an exercise in "non-creative destruction."

According to the psychoanalyst Ron Britton, there is a direct relationship between the 'expectation of understanding the real' and the tolerance of dissent.⁹¹ The higher the expectations (as is often the case in natural sciences), the higher the tolerance of dissent; but if the expectations are low (as in so much of economic analysis), intolerance tends to be high. The economic discipline of post-neo-liberal reforms is a particularly good example of the latter. The opposite is often the case of physics; Einstein, for example, would happily say that he is never quite sure that his picture was the only one which could explain his observations.

Foucault's (1979) conception of the relationship between power and knowledge, particularly the role of economic 'discipline' in democracy —as a form of power that disciplines by imposing specific forms of knowledge— is helpful in understanding the role of the 'experts' in all this: as in Chile, they have become the praetorian guard of neo-liberalism. Their pathetic role in a recent national debate regarding the withdrawal of 10% of private pension funds to help weather the decline of household incomes due to the pandemic is a paradigmatic example

⁹¹ Britton (1998).

of this: they competed among themselves for the most apocalyptic prediction of what would happen if this was approved by parliament. However, since they have been crying wolf for too long, nobody now pays much attention.

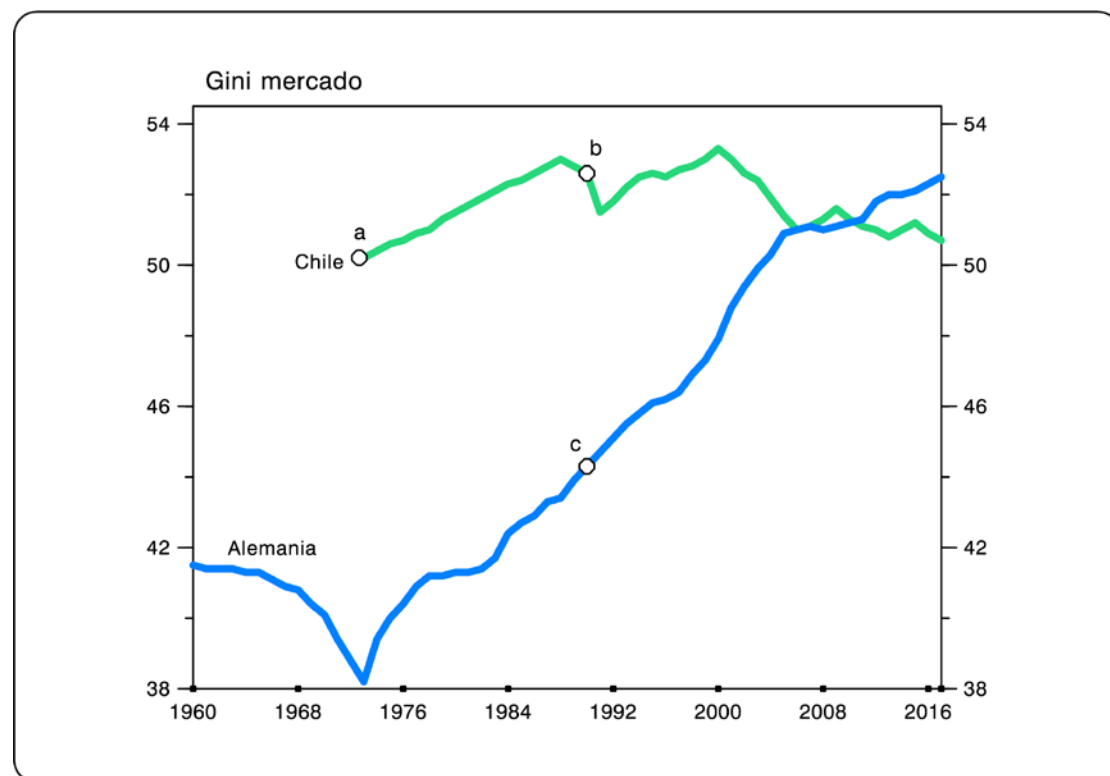
A2.3.- The growing asymmetry between the economic and the social agenda in the European 'new' social democracy

As suggested above, the fundamental problem with the European 'new' social democracy, unlike its post-war version, is that its new economic agenda became totally dissociated from its (more traditional) social agenda, as the former indiscriminately absorbed the neo-liberal economic discourse, while the latter was almost untouched by it.

In addition, as both agendas remain stuck in the past —one was trying to repeat it, the other to repudiate it— they ignored how a new technological revolution and international economic order made it necessary to rethink **everything** creatively. The case of Germany is paradigmatic in terms of the asymmetry of the two agendas; what has happened to its market distribution says it all.

FIGURE A2.1

Germany and Chile on market inequality: a process of "reverse catching-up"?



- Market-Gini=Gini before taxes and transferences; **a**=Pinochet's *coup d'état*; **b**=Chile's return to democracy; and **c**=German reunification.
- **Source:** SWIID (2020). As unfortunately this source (or similar) does not provide information by deciles, it is not possible to work with the methodology of the Palma ratio.

It is remarkable how the election of Reagan and Thatcher, and the fall of the wall, unleashed in the OECD a 'reverse catching-up' with the tropics, "bananising" its market inequality. The Washington Consensus promised "convergence" around the world —and not just in incomes, but also in institutions, inequality, and so on.

And distributive convergence did indeed occur, but it happened in the wrong direction!

The difference between Europe and the US's post-war social democratic economic agenda and the subsequent pro-neo-liberal one is that the former sought to generate economic dynamism by "disciplining" capital, so that the only way it could make money was by doing something socially useful —especially at home. In its version 2.0, however, the new neo-liberal theology ingrained in its "common sense" (Gramsci's perspective) that the only way to generate economic dynamism was through keeping the rich happy. The harmful impact this had in areas such as market-inequality is evident in the figure.

Furthermore, while in Germany the market-Gini jumped by a third, investment fell by the same proportion (it collapsed from 30% of GDP to 20%), becoming similar to the average level of Latin America since 1980; and this obsession with "Latinamericanising" investment became a generalized phenomenon in the OECD. Meanwhile, in Germany productivity growth also collapsed from growing at about 4% to 5% a year to almost zero —again, to a level similar to the Latin American average since 1980.⁹² Not surprisingly, China turned the tables on Germany.⁹³

In other words, in terms of inequality, the 'iron law of oligarchies' seems to be that when one gets a Latin-style, artificially inflated market-inequality the greater the proportion of income appropriated by the top, the lower the proportion of that income that will be returned to the economy in a productive way.

The US, in turn, also became more unequal in its market distribution than its Latin neighbour (Ginis of 51 for the US and 47 for Mexico); and with a President who only lacked dark glasses to look like another banana-republic dictator. If the US had had the same income level as it has now, but the level of inequality from when Reagan was elected, the top 1% would be earning US\$2 trillion less than they do —a figure greater than Brazil's GDP! Meanwhile, the average real hourly wage has been stagnant ever since. Linking this with the above mention issue regarding investment (that in the US over US\$ 1 trillion more would be invested per year if it still had its pre-Reagan investment-GDP ratio), we find a clear "reverse catching up" in motion with countries at the other side of the Rio Grande.

It should be no surprise, then, that when Pope Francis referred to modern-day capitalism, he said that its "unbridled greed" is the "dung of the devil", which creates a "subtle dictatorship", and also plunders nature.⁹⁴ Also, when speaking about financial markets, he added that "A new, invisible and at times virtual, tyranny is established, one which unilaterally and irremediably imposes its own laws and rules".⁹⁵

My criticism of the European 'new' social democracy is not so much for its attempts to absorb elements of economic neo-liberalism —after all, that is a matter for them to choose— but for its inability to do so **creatively**. As

⁹² Palma (2019a and 2020a).

⁹³ According to a *Financial Times* columnist, "Germany once saw China as an export market for machinery with which China would develop its industrial base. Today, China is becoming the senior partner in the relationship. [Germany's] biggest problem is falling behind in the technological race. ... [This] is symptomatic of a fundamental European problem. ... [Now there] are signs that complacency is about to turn into panic". (www.ft.com/content/19fd8544-3c2f-11e9-b856-5404d3811663).

⁹⁴ <https://edition.cnn.com/2015/07/07/world/pope-mass-ecuador-quito/index.html>; see also <https://www.theguardian.com/world/2015/jul/10/poor-must-change-new-colonialism-of-economic-order-says-pope-francis>

⁹⁵ <https://uk.reuters.com/article/pope-economy/pope-rails-against-dictatorship-of-the-economy-urges-reform-idUSL6N0DX27N20130516>

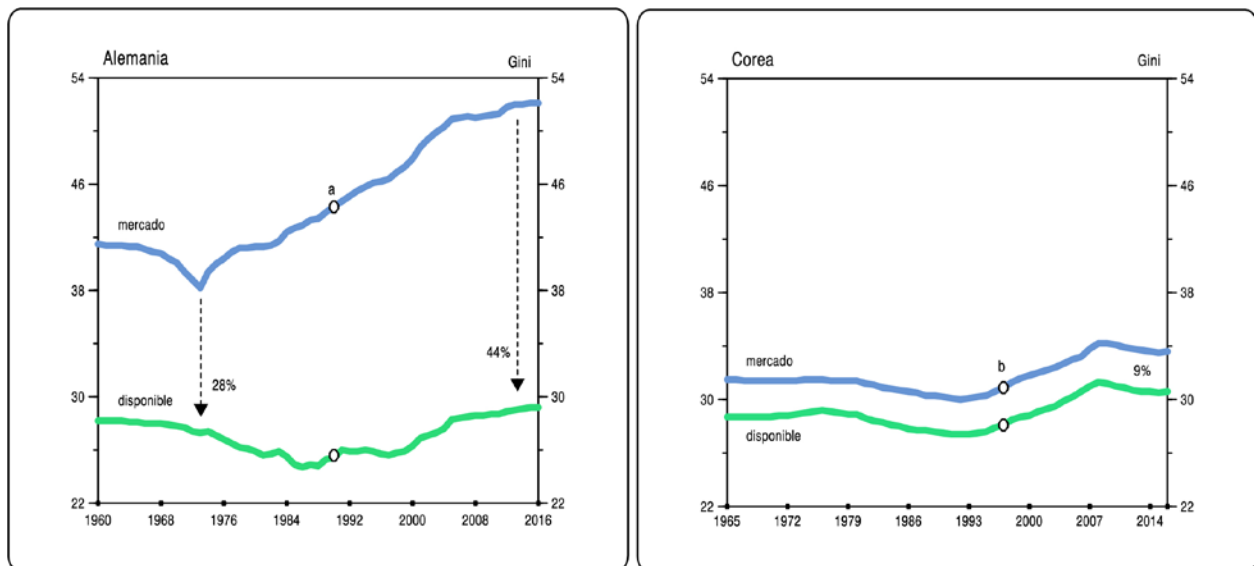
mentioned above, for Gramsci, every hegemonic ideology must absorb elements of opposing ideologies, articulating them with the essence of its own. This is what Chile's neo-liberal ideology did so brilliantly well after the 1988 plebiscite and the return to democracy, and what it is trying to do now all over again in 'strategy 4' to ensure the critical mass of social peace needed so that everything could remain basically as it was (in a 'gatopardian' way).

What happened instead to the European 'new' social democracy was that the effort to absorb elements of its opposing ideology was done unimaginatively and in a sometimes opportunistic way, letting the neo-liberal economic ideology simply replace the existing one. The result was an insipid economic ideology, which was totally disjoined with its more traditional social agenda.

The crucial point is that Germany's bizarre deterioration of market inequality was far from inevitable (or that in the rest of Europe, Western and Eastern). Figure A2.2 compares Germany and Korea.

FIGURE A2.2

Germany and Korea: market vs. disposable income inequality, 1960-2017



- **market**= market-Gini **disposable**= disposable income-Gini (after taxes and transferences); **a**=German reunification; **b**=East Asian financial crisis.
- Source: SWIID (2020).

As the figure indicates, both Germany and Korea arrive at the same final destination —i.e., at the same distribution of disposable income (Gini about 30, or a Palma ratio of about 1.2). However, Korea almost get there already in the sphere of production, while Germany (to keep the rich sweet) **chooses** to follow a tortuous path: while it lets its market-distribution worsen by 14 Gini-points during this period, it then implements a redistributive policy of pharaonic dimensions so as to get to where Korea arrives without much redistribution effort. While in Korea the economic and social agendas point in the same direction, in Germany the two agendas obstruct each other.

This is what I call the European 'new' social democracy's "distributive failure"; and this failure is different from an increase in market inequality *per se* —which is a distributive failure in itself. This new distributive failure relates to the increasingly inefficient, and surely unsustainable in the long run, reduction of market-inequality. It relates to the ever increasing (and economically distorting)

gap between market and disposable income inequality, and the inevitable plethora of market failures, market distortions, transaction costs and increases in public debt associated with it.⁹⁶

The end result of this distributive failure is that the direct requirements for 'social protection' in the European Union already represented 40% of public spending (the equivalent of 16% of GDP) before the pandemic. Furthermore, if one adds public health and education, this total reaches two thirds of all public spending—equivalent to no less than 25% of GDP! With the pandemic, of course, as inequality and the need for social protection have increased, this cost has soared.⁹⁷ In the Eurozone, for example, the budget deficit has grown almost tenfold.⁹⁸

In sum, even before the pandemic, in Germany one out of every four euros of value added had to be allocated to social protection—and mostly to reverse an absolutely unnecessary, inefficient and gigantic Latin-style market inequality.

Pope Francis hits the nail on its head, criticising "a certain liberalism that believes it is necessary first to produce wealth [for the few], **no matter how**, to later promote some redistributive policy by the State".⁹⁹ The key here is in the 'no matter how' part of the quote; not only has Europe "Latinamericanised" its market inequality, but (as mentioned above) its financialised and rentier élite has done the same with investment and productivity levels. If at least the 'how it was done' really mattered (i.e., **without distorting markets**), perhaps even that particular economic dynamic would not have been so inequalising and growth-inefficient, and there would not have been such a need for social protection, and so the redistributive cost might not have been of such unsustainable dimensions.

Korea, on the other hand, only needs to invest 11% of GDP in social protection to reach the same distribution of disposable income for which Germany has to spend more than double. That is why Korea can afford two simultaneous treats: collecting 15 percentage points of GDP less than Germany in taxes, and also having double Germany's level of public investment.¹⁰⁰

This is why the European 'new' social democratic welfare state has ended up *de facto* being a subsidy to market inequality, since such high inequality would not have been feasible without both the mammoth (and perfectly avoidable) level of taxation, and the explosion of public debt. Apparently, social protection is a subsidy for the poorest, but in reality the biggest beneficiaries of this social protection are high-income groups. This level of social protection not only makes such market inequality politically feasible, but also after the 2008 financial crisis, for example, the US and Europe spent US\$1trillion on bank bailouts, and US\$15 trillion were injected via "QE" (quantitative easing) into financial markets so as to sky-rocket the net worth of a few individuals.¹⁰¹ Bringing us back to the already mentioned issue of the post-modern Robin Hood (who not only robs the poor to give to the rich, but also robs the rich to give to the very rich).

⁹⁶ For a detailed analysis of this issue, see Palma (2019a).

⁹⁷ On the rapid increase of inequality during the pandemic, see <https://www.ft.com/content/ab30d301-351b-4387-b212-12fed904324b>; see also Palma (2020b).

⁹⁸ <https://www.ft.com/content/5579361f-5aac-4cd3-9e93-190fffdc0baf>

⁹⁹ <https://www.lanacion.com.ar/el-mundo/papa-nid1772302/>. Emphasis added. I would like to believe that the resemblance between his stress on the 'no matter how' part of the story, and my own emphasis on that particular factor in my work is not coincidental as one of his advisers told me that he had passed my work on inequality to him...

¹⁰⁰ OECD (2020a).

¹⁰¹ Palma (2020b).

And to continue my comparison between Latin America and some more enlightened East Asian countries, while Korea spends the same as Chile in social protection (11% of GDP), with that expenditure it manages to get to a disposable income-Gini of 30 while Chile only manages one of 48. Taiwan, meanwhile, spends even less, and reaches an even better destination. And Brazil spends more than twice as much as Korea and Chile in social protection (although half of that is just clientele subsidies to pensions, an amount that is larger than overall public spending in health and education)¹⁰², but only achieves a level of inequality in disposable income that is even worse than Chile's (a Gini of 51). As for Mexico, it spends and achieves little —it spends less than 8% of GDP on this, and ends up with a Gini of nearly 44.

Thus, Latin America subsidises inequality doubly: first, like Germany, it allows its oligarchy to distort markets at will; but then (unlike Western Europe), it only taxes at half Germany's level, making it impossible to arrive at a more civilized distribution of disposable income.

¹⁰² IPEA (2019).

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